RESALE PRICE MAINTENANCE

BY

CLAUDIUS TEMPLE MURCHISON, A. B.

Sometime Lecturer in Economics, Columbia University
Assistant Professor of Economics, Hunter College, New York

SUBMITTED IN PARTIAL FULFILMENT OF THE REQUIREMENTS
FOR THE DEGREE OF DOCTOR OF PHILOSOPHY
IN THE
FACULTY OF POLITICAL SCIENCE
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Dedicated

TO

MY MOTHER

PREFACE

Many investigations and much argument are at the service of the student of price maintenance. They spring from various sources a few of which are: trade associations and trade papers; chambers of commerce, including the National Chamber of Commerce; the Federal Trade Commission; the Committee on the Judiciary of the House of Representatives; the Interstate and Foreign Commerce Committee of the House of Representatives; the American Economic Association; the American Academy of Political and Social Science; economic journals; and numerous business experts and economists such as P. T. Cherington, F. W. Taussig, H. R. Tosdal, A. W. Shaw, P. H. Nystrom, R. S. Butler, Lee Galloway, Gilbert Montague, and Judge Brandeis. Much information has been gleaned from the evidence offered to the Federal Courts in the course of the abundant litigation over price maintenance. Unfortunately, however, much of the available data on the subject has originated from biased sources. Indeed, almost no important assertion of fact has escaped the charge of being either wholly false or intentionally exaggerated. Under such conditions the problem of evaluating evidence is extremely difficult. Engaged therein the most impartial and conscientious student is not entirely immune to deception.

The arguments and conclusions presented in the following pages are given with no assurance of finality. They favor neither the negative nor the affirmative side of price maintenance. Long study has convinced the author that neither side is wholly wrong nor wholly right. A compro-

mise solution seems inevitable. The reader should take note that the treatise is far more concerned with establishing the *principle* of compromise than in constructing any particular form of compromise. Though a form is suggested, it is done in the knowledge that first solutions are generally ill-fated. But what of it, if they serve in the capacity of prerequisites for those that succeed?

The author desires to express grateful acknowledgment to those who have so kindly advised and criticized in his preparation of this work. Especially are his thanks due to Professors Seligman, Seager, McCrea, and Haig of the Columbia faculty, and to Professor Cherington of the Harvard School of Business Administration. In fairness to them it should be said that the study falls far short of the attainments suggested by their constructive criticisms, and it is by no means entirely freed of all the faults which they indicated. Its defects are attributable only to the shortcomings of the author himself.

C. T. Murchison.

New York, March, 1919.

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CHAPTER I

The Organization of the Market

The problem of price maintenance would be simple enough of solution if it could be isolated and studied apart, after the manner of a star-fish or an aching tooth. But it refuses to be isolated. Its ramifications extend far and wide, permeating every nook and corner of our marketing system from the producer furthest removed to the most ultimate of ultimate consumers. A correct mental image of the marketing system as a whole must then be prerequisite to a proper understanding of the merits or demerits of price maintenance itself.

A manufacturer today may use at his discretion one or more of several trade channels in the transmission of his goods from the factory to the consumer. The most popular one is the manufacturer-jobber-retailer route. However, many goods are sold directly to the retailer by the manufacturer without the services of the jobber. To a small but increasing extent goods are also sold directly to the consumer from the factory, through the use of the mail-order system, or manufacturers' stores, or agencies.

Formerly the trade channels were more complicated and were generally traced as follows:

1. Manufacturer.
2. Commission merchant.
3. Jobber.
4. Wholesaler.
5. Retailer.
6. Consumer.

This condition, however, is not typical of modern marketing. Better transportation facilities; better co-ordination between the factors; the principle of more rapid turnovers; more and better advertising; a growing response on the part of the masses to seasonal influences in demand; rapid changes in styles; fads, hobbies—all contribute mutually to the simplification and shortening of the road between factory and consumer. The commission merchant is now to be found in only a comparatively small number of industries; the functions of jobber and wholesaler have been practically merged, so that it is a matter of indifference as to whether they be termed wholesalers or jobbers. It has been estimated that 90 per cent of all groceries and a somewhat less proportion of other lines pass through the manufacturer-jobber-retailer channel.[1] Let us study briefly the functions of each of these marketing factors.

The Manufacturer. For the purposes of this treatment those manufacturers only need be considered whose products are of the finished variety, that is, ready to be passed on to the ultimate consumer without any further alteration. Moreover, their products must be of the type which is readily identifiable, either because of inherent form, function, or quality, or because of special markings, labels, or cartons associated with them. The problem of price maintenance, then, does not touch the farmer as a producer of wheat, but it does touch the miller as a manufacturer of flour, if he attaches to the flour a distinctive brand or trademark. If, however, he sells the flour in bulk to be branded or otherwise identified by, or in the name of, some jobber or retailer, he is not concerned with price maintenance. The same rule applies to a baker as a producer of bread. The problem of price maintenance does not seriously concern a

[1] Butler, *Marketing Methods*, pp. 32-33.

fruit-grower who sells his fruit in bulk, but does concern one who sells his fruit under a definite brand, or in distinctive wrappings.

A packer who puts meat and fat on the market simply as ham or lard is not interested directly in price maintenance; but a packer whose hams are trade-marked and whose lard is branded has a different attitude.

Having identified the type of manufacturer concerned with the problem, let us now outline the rôle he plays. In some cases his campaign is comparatively simple. He merely turns over his entire product to some sales company, or jobber, who agrees to assume all selling responsibilities. This leaves the manufacturer free to confine his attention to producing. The great majority of manufacturers are not content with any such arrangement, however. Big profits and rapid extension of business do not often come when the fate of the commodity is so completely in the hands of a less interested second party.

Should he desire to take a more responsible rôle in the selling process, he will probably choose one or more of the following methods: [1]

A. From the manufacturer directly to the consumer. There are three possible variations of this direct route:
   1. Through solicitors or canvassers who visit the consumers personally.
   2. By use of the mails.
   3. Through the manufacturer's own retail stores, usually conducted on the chain-store principle.

B. From the manufacturer direct to the retailer.
   1. The manufacturer may reach the retailer through salesmen, or by mail.

[1] Butler, *Marketing Methods*, ch. iii.

2. He may deal with all types of retailers, or choose one or more of the following types:
   (a) Country general stores.
   (b) Specialty stores.
   (c) Department stores.
   (d) Chain stores not owned by the manufacturer.
   (e) Mail-order houses.
   (f) Co-operative buying organizations of retailers.
3. He may sell generally to all retailers in a selected class or he may confine his sales to one retailer or a few retailers in a community, regardless of class.

C. From the manufacturer directly to jobbers.
1. He may reach the jobbers either through salesmen or by mail.
2. He may deal with all jobbers who will co-operate with him, or
3. He may deal with selected jobbers in restricted territories.

D. From the manufacturer directly to special representatives.
1. Agents,—those having charge of extensive territory, marketing the goods through subordinate middlemen.
2. Commission men.
3. Brokers.

These special representatives all usually have the option of selling to jobbers, retailers, or consumers.

Whether a manufacturer is to sell through one or more of these channels, whether he is to use salesmen or the mails, or both, depends partly on custom in the trade, partly on

the nature of the product, partly on his own ability to discover methods of marketing, and to adapt to his own use all marketing plans that appeal to him as offering new opportunities for the sale of his goods.

Should he choose the method of direct sales to consumers, he has the advantage of knowing just where his goods are being consumed, and hence can the better direct his advertising and sales efforts; he has absolute control of his market and, therefore, has no difficulties with price-cutting, substitutes, or lack of dealer co-operation. An offset to these advantages is found in the great expense of direct selling in most cases, and the antagonism of dealers who feel that the manufacturer is assuming a function properly theirs.

Should he choose to sell to retailers he will find it necessary to keep on the road at great expense large numbers of salesmen, or else to create the necessary good-will for his products by heavy advertising. Moreover, a large percentage of loss results from having to give credit accommodations to so many individuals many of whom are entirely unknown to the manufacturer as to honesty, financial standing and business ability.

But there are compensating advantages. Where the manufacturer deals with the retailer, the problem of price maintenance can be handled with a large degree of success. Moral pressure can be brought to bear more directly, or else the retailers may be relegated to the position of agents handling the goods on consignment, and therefore compelled to maintain the price. The manufacturer's salesmen meet the retailers personally, have an opportunity to educate them regarding the selling qualities of the goods in question, and perhaps can impart to them real interest in and enthusiasm for the goods. He may, moreover, choose to do business only with those retailers who will give the goods prestige and wide distribution.

Four general types of commodities are still for the most part entrusted to jobbers, namely: dry-goods, groceries, hardware and drugs. Moreover, jobbers are of great service in the handling of thousands of other commodities not so classified. The real jobber is one who buys goods in large quantities, transmitting them without alteration in smaller quantities to the retailers. Aside from this conventional type is the jobber who manufactures, and the jobber who sells not only to retailers but also to consumers. These last two types are playing an increasingly important rôle, but they will not be taken up for discussion until later.[1] In selling to jobbers, the manufacturer need use only a relatively small sales force, as the jobbers, compared to the retailers, are of course few in number. For the same reason he is troubled with less bookkeeping, his credits are more concentrated and reliable, and his shipping costs are less, as a result of fewer but larger shipments.

Many people claim that the jobber is a superfluous factor in the marketing system, that his functions can be assumed and performed more economically by other agencies. The facts hardly bear out this contention. For in the first place the jobber is a specialist, a selling specialist. The machinery of his organization is shaped and directed to attain one goal only—maximum sales at minimum cost. His energies are not dissipated.

Secondly, the jobber holds an advantage in that he handles a variety of goods, far greater than can be put on the market by any single manufacturer. The items on his selling list are often numbered by the thousands. This fact achieves economies in several ways. (1) He can supply entirely the needs of the average specialty store. Thus the retailer receives his goods in fewer but larger, and hence more economical, shipments. (2) A

[1] *Cf. infra*, p. 59 *et seq.*

smaller number of salesmen suffices. Let us assume that the goods in an average specialty store are produced by five hundred different manufacturers—a conservative estimate. Were each manufacturer to do his selling through his own salesmen, it is easy to see that the resultant aggregate costs would be exceedingly high. But with the selling activities of all pooled, so to speak, in the person of the jobber's salesman, one man does the work of many. (3) The jobber can, and generally does, with good profit, confine his selling to a comparatively small territory. The manufacturer with his specialty must needs make his attack on the country as a whole. This wide distribution of effort entails a heavy unit cost, if the manufacturer takes the whole burden on himself. The concentration of selling within a limited territory is then a practice of which advantage can be taken in most cases only by the jobber. (4) The variegated stock of the jobber enables him also to perform economically the function of warehousing. This relieves the manufacturer of the necessity of keeping on hand a large surplus, and enables the retailer to secure virtually at any time, without previous notice, desired additions to his stock.

Thirdly, the jobber, by virtue of his extensive and continued dealings with the retailers of a limited territory, comes to know them well as to ability, honesty and financial standing. Thus he is in a position to manage his credit, giving wisely and safely. This has constituted a very large advantage for the jobber in the past. It seems certain, however, that it will diminish somewhat with the growing use of the trade acceptance, and the institution of better business methods in general.

In the light of these facts we must admit that the foundation of the jobber is a fairly solid one and will not easily yield to such developments as the chain-stores, the department stores, the mail-order houses, the co-operative asso-

ciations, and others.[1] But these considerations must await a following chapter for fuller discussion.[2]

Direct sales to special representatives, the last of the trade channels mentioned in the skeleton outline, occur when the manufacturer chooses to forego as much selling responsibility as possible. This attitude may be occasioned by, (1) limited capital; (2) limited demand, not large enough to justify other arrangements; (3) unfamiliarity with the market, due to lack of means or disinclination to learn; (4) peculiar organization of the market which in some cases requires the use of brokers, as, for instance, the selling of stocks, bonds and produce.

Having thus traced, all too briefly perhaps, the problems and selling activities of the typical manufacturer who is interested in the question of price maintenance, let us once more turn our attention to the jobber.

The jobber. As we have seen, probably ninety per cent of the country's groceries, and overwhelming proportions of many other lines of consumer's goods, are handled by jobbers.[3] Of the jobber's stock, a large proportion is of the branded or trade-marked variety. It is to his interest, then, that the goods maintain a popularity on the market. In other words, his reputation and prosperity are in exact proportion to the reputation and demand for the goods he carries. All jobbers admit this. But all jobbers do not agree as to the selling policy that makes for reputation and demand. For some jobbers no selling methods are too aggressive. In striving for big volume and rapid turn-over they indulge in liberal price-cutting on many articles, and in addition grant generous quantity discounts to large buyers.

[1] A. W. Douglas, *Merchandising, passim.*

[2] *Cf. infra,* p. 68 *et seq.*

[3] *Cf. supra,* p. 12.

Others believe that sound business goes with a maintained price and a conservative discount policy, and depend on service, reliability and other virtues to assure a large and growing trade. Some oppose national advertising as practiced by many manufacturers on the ground that the resultant large demand for the good compels the jobber to carry it, whether or no, and that, as a consequence, the manufacturer is arbitrary and often miserly in the granting of jobbers' discounts. Some jobbers sell directly to consumers in competition with retailers, thus taking an extra large profit to be sure, but arousing the wrath of all his customers. Large numbers of jobbers have transgressed the traditional boundaries of the wholesaling function by integrating in an opposite direction and assuming the rôle of manufacturer. The manufacturing jobber is becoming an increasingly important factor in the marketing system. A great majority of his products do not originate in his own plants but are manufactured under contract by others, always bearing in the market, however, the brand and name of the jobber. The jobber's brand so used is popularly known and spoken of as the "private brand." Goods of private brand, having generally a restricted distribution, do not readily lend themselves to price-cutting schemes. Moreover, they possess advertising value, and may add greatly to the prestige of the jobber in the market. Discussion of the private brand as it affects the price-maintenance problem is reserved until later.[1]

In relation to his competitors the jobber occupies a position far different from the analogous position occupied by the manufacturer. Any manufacturer of any branded commodity in competing with manufacturers of similar commodities for the market, is always in a position to plead superiority of quality, or of form, or of variety of uses, or of

[1] *Cf. infra*, p. 59 *et seq.*

service, durability, and innumerable other real or imagined superiorities. He does not have to specialize on a price appeal. All questions of price can often be entirely subordinated.

Not so with the jobber. Any given jobber in any given line carries in his stock just what any other given jobber in that line carries. It does not lie in the province of any jobber to say that his Pear's Soap is superior to the Pear's Soap carried by all other, or that his Heinz products are of a peculiarly succulent quality. Wherein, then, can one jobber find advantages that will enable him to triumph over his competitors? He may possess a strategic location, capable salesmen, financial backing, wisdom in buying, skill in exercising economies of various sorts. He may give liberal credit, good service, kindly co-operation, and be famous for square-dealing. But with all these, the temptation to make the price appeal is always present. How easy it is to cut a few cents per case on Cream of Wheat, to lower the standard price just a little of Welch's Grape Juice! How immediate, how certain the results! For the time being he is almost certain to prosper. In the long run, perhaps, the story is different, because the other jobbers will not be slow to take the cue. In the price-cutting game there is no limit to the number of players or to the size of the stakes.

Retailers.[1] The retailer is the last link in the chain of middlemen. He sells to the ultimate consumer, without alteration in form, the goods purchased from jobber or manufacturer. He gives to the goods time and place utility. Retail stores may be divided into specialty stores and general stores. The former handle goods of one particular line, or

[1] *American Economic Review*, June, 1917; "Marketing Functions and Mercantile Organization," L. D. H. Weld.

of several closely related lines, as, for instance, drug stores, groceries, shoe stores, music shops. The latter deal in varied and numerous lines. Such are the old-fashioned country stores which contribute to all the needs of the community, or the modern department store or mail-order house where one can buy anything from toilet goods to gas engines. From another point of view, retailers may be classified as follows: chain stores, mail-order houses, department stores and consumers' co-operative stores, the others being rather vaguely alluded to as the " average independent retailers."

The selling methods of retailers vary greatly. Some afford to their customers elaborate accommodations, parlors, lounging rooms, finely-appointed sales rooms, music recitals, luncheons, fashion displays, etc. Their practice varies as to credit accommodations and the privilege of returning goods. Some stores deliver the goods to the homes of the customers, and even transport the customers themselves; others, of course, do neither. Some engage in extensive advertising, the giving of premiums, coupons, trading stamps; some make a habit of cutting standard prices. Some cater exclusively to the wealthy, some to the middle classes, some to the poor. The resplendent department store, with its gorgeously dressed windows, its luxuriant and expensive furnishings, its numerous and immaculately dressed sales corps, may not be two blocks distant from the humble shop where windows are for lighting purposes only, where pine boxes serve as counters, and where the unkempt proprietor is his own clerk, bookkeeper and janitor. Apart from the selling function, the only universal characteristic to be found among retailers is that all of them handle large proportions of branded or trade-marked goods, and hence would in nearly all cases be affected in some way by a price-maintenance program. Retailers vary not only as to characteristics and general selling methods, but also in their buying.

Not all buy largely from jobbers. Some buy in large quantities, some in small, some pay cash, others always depend on credit; some believe in a variety of goods, others stock up only in staples. Some utilize co-operative associations for their buying, some prefer to buy independently.

These considerations taken in connection with many other varying business methods lead one to the conclusion that, as regards retailers, types are very numerous. Therefore costs and profits among retailers must be widely variant. In the beginning, then, one is disposed to wonder how a rigid price-maintenance formula can be adapted to so irregular and inconstant a system as is required by the present methods of commodity distribution.

By way of summary, we may conclude as follows:

1. The problem of price maintenance is directly connected with the marketing of only branded or trade-marked goods.

2. Manufacturers have at their disposal a large variety of methods by which to reach the buying public, though the one most generally used is that of distributing through jobbers and retailers.

3. Jobbers vary greatly as to types and selling methods. We find price-cutting, quantity discounts, private brands, aggressive selling, all being regarded differently. Hence the variations in the cost of operating are large.

4. What is true of jobbers as to variations in method and costs is true to a still greater extent of retailers.

5. Both jobbers and retailers handle large proportions of trade-marked and branded goods.

6. Each jobber and each retailer is in such relation to his competitors that the temptation to cut prices, in order to gain a competitive advantage, is ever present.

7. Because of the intimate contact existing between all members of a competitive group of jobbers or retailers, any

selling device, such as price-cutting, if practiced by one, seriously affects the business policies of all.

8. A close interdependence still exists as between retailer and jobber, and between jobber and manufacturer. The prosperity of one contributes to the prosperity of all. But this close interdependence leads to an additional result: whenever trade-marked or branded goods suffer in reputation or distribution through the act of one set of factors, they suffer likewise in the field of the other factors.

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L. D. H. Weld, "Marketing Functions and Mercantile Organization," *American Economic Review*, June, 1917, pp. 306 *et seq.*

CHAPTER II

Statement of the Problem

The immediate occasion of the price-maintenance controversy lies in the general tendency toward the broadening of the functions of the manufacturer. Formerly they were confined, as a rule, to the creation of a finished product, the marketing responsibility devolving almost entirely upon other agencies. Such selling activity as the manufacturer did assume generally restricted itself to dealings with wholesalers or jobbers. In recent years a majority of those manufacturers who produce commodities for the retail trade have widened their activities to include not only marketing to wholesalers but to retailers and consumers. Though in most cases the manufacturer retains the services of the middlemen as channels of distribution, he does not entrust to them nearly so great a degree of responsibility as he once did.

This change of attitude on the part of the manufacturer under discussion is due to no fundamental psychological change, but to the removal of certain economic limitations under which he once labored: namely, difficulties of transportation and communication. Inadequate or relatively too expensive transportation facilities made it impossible for the average manufacturer of one product or of a small variety of products to maintain a large sales organization or attempt a wide distribution. Poor communication facilities, expressing themselves in slow or irregular mails, limited telephone and telegraph communications and a lack of

widely circulated periodicals suitable as advertising media made it hopeless to attempt the building-up of a wide demand by appealing directly to the consumer or to the small dealer.

With the elimination of these difficulties it is not surprising that the manufacturer should take advantage of the open opportunity to create a wider market by his own efforts and at the same time to achieve a position of greater advantage relative to his distributors. Advertising, for so long a local device financed by dealers, in the hands of the manufacturer becomes national in its scope. Periodicals of national circulation become one of its most popular vehicles, and are in turn given great impetus both in numbers and in wideness of circulation by the financial support of the advertisers. By a single manufacturer great sales organizations are developed with tentacles reaching into the remotest sections. National periodical advertising is accompanied by a greater use of other forms such as circulars, posters, and catalogs. Utilization of the device, once its possibilities in the creation of demand are realized, rapidly develops into a science possessing a complicated psychological basis.

Many modifications of the old system of commodity distribution have occurred in consequence. In a majority of cases such modifications have accorded to the manufacturer a greater degree of control over the final marketing of his products, and a greater responsibility in the creation of consumer demand.[1]

A necessarily parallel development has been the almost universal adoption by specialty manufacturers of commodity standardization. Each unit of the product is made similar to every other unit, not only in its physical characteristics, but even in its wrapping or carton. Then to accen-

[1] Nystrom, *Economics of Retailing*, ch. ii; Butler, *Marketing Methods*, chs. ii and iii.

tuate the degree of uniformity a common brand or trade-mark is affixed. The advantage of standardization from the manufacturer's point of view is twofold. It permits greater uniformity and definiteness in advertising, and at the same time enables the manufacturer to make sure of delivery to the consumer, through dealer channels, a commodity which corresponds exactly with the claims set forth in the advertisement.[1]

As a further aid in marketing, many manufacturers insist upon supplementing commodity standardization by price standardization. They claim that this enables the manufacturer to emphasize not only certain utilities, but also attractiveness of price. Often the price appeal is the deciding factor in securing a sale. The best moment for its presentation may well be at the time when the potential customer is interested in the advertisement. With respect to the old customers, too, there is a strong appeal in the one-price-to-all policy, especially so if there be present the conviction that the one price always commands in an unvarying way the utilities desired. As the reputation of a standardized good increases the price naturally becomes associated in the consumers' minds with the other characteristics which regularly identify the good.[2]

Should the qualities of the commodity and its price become widely and favorably known, it becomes peculiarly susceptible to price-cutting. It is said that the public having associated for a long time a given commodity with a given price will readily detect a lowering of price and respond thereto. Advantage of this fact would naturally be taken by an occasional dealer on the theory that the cut price would be a fine competitive weapon. To be sure, this does not

[1] Nystrom, *op. cit.*, pp. 268-269.

[2] *Ibid.*, p. 256.

explain all cases of price-cutting, for there are many other causes which bring it about. As a result of price-cutting the manufacturer professes to see a chain of evils. First, competing dealers must meet the cut to retain their trade, which means sacrificing all profits in the commodity, or even entailing financial loss. Second, the discounted goods lose popularity with the dealers who if they continue handling them at all, do so only with reluctance. Third, the public is deprived of the commodities altogether, or else is able to get them only with difficulty, being compelled in most cases to accept unsatisfactory substitutes. Fourth, the manufacturer by the disruption of the market through no fault of his own is subjected to heavy financial losses, and continues business only with the greatest difficulty.[1]

To prevent price-cutting, manufacturers have in the past resorted to many different devices. The chief of them are as follows:

First. The manufacturer grants to such dealers as are willing to maintain the fixed price a liberal rebate on the list price, such rebate payable only when the goods are sold. Any variations from the fixed price entail forfeiture of the rebate. As the margin of the retailer's profit, exclusive of the rebate, is purposely narrow, the loss of the rebate means a financial loss on all the commodities involved.

Second. Many manufacturers have made a practice of refusing to sell to those dealers who cut prices below the standard. Some have gone so far as not only to refuse to supply the offender, but also to bring pressure to bear on all jobbers and retailers to refuse to supply him—thus making it impossible for the price-cutter to renew his supplies from any source.

[1] *Hearings before Interstate and Foreign Commerce Committee* (House), Jan. 5-11, 1917, pp. 476-483.

Third. Prices have been maintained by causing to be incorporated in all contracts of sale special provisions by which the dealers bound themselves to observe a fixed price.

Fourth. The making of conditional sales. In these cases title to the goods sold to dealers remained in the manufacturer, and passed to the dealers only upon the consummation of the resale made at the fixed price. The manufacturer reserved the right to demand the return of all unsold goods, upon the failure of the dealer at any time to maintain the price.

Fifth. The use of a license agreement whereby the dealer is regarded merely as an agent or demonstrator without title in the goods. As agent he must sell at a stated price. His profits are in the form of commissions.

Sixth. By affixing to the good or its container, or printing thereon, a statement to the effect that a certain price must be observed, the implication being that the use of such a notice made of the transaction a conditional sale, which bound the dealer to the price fixed.

Seventh. A claim on the part of the manufacturer of patented or copyrighted goods that the usual patent or copyright rights included the right to fix a resale price and to compel the observance thereof.[1]

Virtually all these methods have been adjudged illegal by the Federal Courts, and in so far as they still exist, they are merely nominal. Seemingly no dependable price-maintenance weapon is left in the hands of the manufacturers. It is generally thought that the elimination of price-cutting can be achieved only by Federal legislation. Such legislation has been proposed in the form of the well-known Stevens bill. Inability to get favorable congressional action on this

[1] Gathered from U. S. S. C. decision in Boston Store of Chicago *v.* American Graphophone Co., March 4, 1918.

bill has resulted in a campaign for its modification. In its official form it provides, generally speaking, as follows:

I. In any contract for the sale of trade-marked or branded goods the manufacturer may require the observance by dealers of a fixed price, provided that he has not a monopoly of the articles belonging to the same general class of merchandise, that his brand or trade-mark is registered with the Federal Trade Commission, together with the price-lists and other conditions to be enforced, and that such contract permits a limited number of seasonal or disposal sales—two a year—in case the manufacturer does not choose to repurchase the goods himself on thirty days' notice.

II. Emergency circumstances such as bankruptcies, fires, deterioration of goods, etc., may justify divergence from price, provided the manufacturer after thirty days' notice does not care to repurchase the stock.

It may be said of the bill that it accords to the manufacturer unlimited control over the resale prices of his goods, and that the dealers even in the presence of special and serious emergencies may be restrained from price-cutting for a period of thirty days pending investigation and approval by the manufacturer.

The manufacturer who desires the power of price maintenance professes to see in this bill the following advantages: 1. it will prevent the economic evils which result from price-cutting; 2. it will by safeguarding the interests of the manufacturer enable him to devote his energies to more economical production, and thus make possible for the public better values at less price.[1]

The manufacturers are joined in their advocacy of price-maintenance legislation by many dealers, both jobbers and

[1] *Hearings, op. cit.*, Feb. 27, 1914 to Jan. 9, 1915, pp. 120-139; Nystrom, *op. cit.*, ch. xv.

retailers. The latter see in the device the advantage of greater stability of prices. Sharp price fluctuations eliminated, the perils of merchandising would be largely removed and competition would then involve service and efficiency rather than prices. With the standard price, selling is simplified and profits are virtually assured. Also the dealer values the national advertising which is financed by the manufacturer and thought to be dependent on the maintenance of a standard price.[1]

Price maintenance would also diminish largely the fears entertained by some of the small retailers resultant upon the growing powers of the modern giants in retailing, the chains, department stores, and mail-order houses. It is maintained that these owe their development not essentially to economic superiority, but to their command over large capital funds united with their policy of price-cutting which is destructive of competition.[2]

Voices from among the consumers are also heard in behalf of price maintenance. They emphasize the advantage to the consumer of standardized commodities and their easy availability in the market. Their attitude is based on the assumption that there is a vital connection between standardized goods and price maintenance.[3]

The opponents of price maintenance make an issue of the facts on which the affirmative arguments are based. They deny that price-cutting has the disastrous effects claimed, and attribute the disappearance of certain commodities from the market and the embarrassment of certain manufacturers

[1] Butler, *Marketing Methods*, pp. 318-319; Cherington, *Advertising as a Business Force*, ch. xii.

[2] *Hearings, op. cit.* Testimony of Louis Brandeis, pp. 1-72. Testimony of Mr. Zimmerman, pp. 88-108.

[3] *Hearings, op. cit.*, May 30 to June 1, 1916, pp. 184-195; *Hearings of the Committee on the Judiciary*, 1914, pp. 726, *et seq.*

not to price-cutting, but to inferiority of values offered or to general inefficiency. Also they deny that price-cutting is reprehensible in motive and assert that it is a practice which is not only thoroughly legitimate and ethical, but actually necessary at times for economic reasons. Should price-cutting be eliminated it would mean injury to themselves and to the public.[1] Furthermore, they profess to see in the use of the fixed price, coupled with the enormous amount of national advertising which it engenders, an unwarranted encroachment upon the legitimate functions of the retailer.[2]

The opponents also entertain fears that the maintained price under legal sanction would speedily develop into monopoly price. The public would suffer through a higher cost of living, and the dealer through arbitrarily limited profits. Moreover, with the dealer subordinated to the manufacturer in the matter of prices, it would be but a short step to complete control over the distributive system by the manufacturers.[3]

If these opposing arguments do not serve to clarify the problem, they at least indicate its general nature and magnitude.

[1] *Hearings before Int. & For. Com. Com.*, Jan. 5-11, 1917, pp. 11-38, 79-80, 121-140.

[2] *Hearings, op. cit.*, pp. 79-80, 109-110, 197-199, 211-215.

[3] *Hearings, op. cit.*, pp. 97-108, 113, 124-132, 136 *et seq.*, 207, 237, 283-285, 287-310; *American Ec. Rev.*, March, 1916, "Price Maintenance," by F. W. Taussig; *ibid.*, vol. viii, pp. 28-47, 283-305. Articles on "Price Maintenance," by H. R. Tosdal.

CHAPTER III

Types of Price-Cutting: Motives and Reactions

The practice of price-cutting is one at present so familiar to the general public that a definition of it seems needless. It is generally found wherever competitive conditions exist, and the extent of its use may be said to vary directly with the intensity of competition. It is, for the most part, confined to those goods which bear a trade-mark, or the name of the producer. They are goods which are easily identifiable, which are more or less well-established in the market, and which have customarily brought a well-known standard price. Just why such a type of goods is chosen for price-cutting will appear later on.

For purposes of classification, we may mention two general kinds of price-cutting, *direct* price-cutting and *indirect* price-cutting. The former denotes merely a decrease in the usual selling price of a good. The latter denotes that type of price-cutting characterized not by a decrease in the marked price but by the giving free with each purchase such articles as trading stamps, coupons, and various kinds of premiums. The use of this indirect form has become prevalent within recent years. Its economic effects are obviously similar to those of direct cutting, and hence must not be ignored.

With respect to direct price-cutting, another classification must be made. There is a considerable difference between "below-cost" price-cutting and "profit-yielding" price-cutting. Accordingly, for greater accuracy and definiteness in the discussion, we shall call the practice of selling goods

below their actual cost "below-cost" price-cutting. But where the price at which the goods are sold, although cut below the usual price, is yet sufficient to afford the seller a fair profit, we shall use the term "profit-yielding." It is readily seen, then, that the difference between the two categories is one of degree only. Yet the distinction is an important one, as we hope to make evident in the following pages.

Let us now attempt to discover the driving forces which are the immediate cause of price-cutting. The evidence of the retailers themselves will suffice.

There is in the city of New York a department store, especially noted for its price-cutting.[1] In justification of this practice, the store asserts that it conducts its business more efficiently than the majority of its competitors, that it has developed and does exercise economies which other stores lack. For example, (1) it gives to customers no credit accommodations. Every sale is a sale for cash. Hence no losses are suffered through bad debts, idle book capital, and the expenses of a large accounting and collecting force. (2) In the variety and quality of goods, and in their display, it believes that it has another advantage. (3) Its salesmen are of a high order of ability: they secure an unusually high percentage of possible sales, make for satisfied customers and a very small proportion of returned goods. (4) It buys its goods in large quantities, and pays cash, thus securing the benefits of both cash and quantity discounts. Many of its goods are bought directly from the factory. The prices for them do not include any middlemen's profits. (5) It advertises wisely and on a large scale, and has developed a volume of business which in proportion to the capital involved, is far greater than the average. Such rapidity of turn-over can

[1] *Publisher's Weekly*, Apr. 3, 1915.

easily bear heavy price-cutting. For even though the margin of profit on each turn-over be small, a sufficient number of turn-overs will guarantee in the long run large profits.

There is a system of chain stores which not only lays claim to the above economies, but to this in addition: it makes no deliveries to customers. The buyer himself must take home the goods he has bought.[1]

There are other stores which claim the advantage of low rents, and low wage expenditures. Still others enjoy close proximity to buying and manufacturing centers, and hence save on transportation charges.

Such instances could be multiplied *ad infinitum.* Those given are sufficient, however, to make clear that many stores do exist which through peculiar advantageous economies enjoyed by them are able to sell their goods—not one good, nor yet only a few goods of the standard trade-marked variety, but *all their goods*—at a uniform cut-price, and yet derive handsome profits. In such cases there is undoubtedly some economic justification for price-cutting. From these economies which so greatly benefit the stores, why should not the consumer also profit? Bear in mind that at this point the only price-cutting considered is "profit-yielding" price-cutting. No article is sold at a price which affords no profit.

Now for a glimpse of the price-cutters in the other category. Their price-cutting is not only unjustified by the enjoyment of economies of any sort, but is moreover of the type known as "below cost." Their motive in price-cutting, then, cannot be merely to transfer the benefits of economies to the consumer, but is chiefly to advertise. It is advertising which does not inform the public as to the merits of any particular commodity. It only informs them that certain

[1] See *Journal of Commerce*, Oct. 18, 1915, p. 13. "The Economy Store Plan."

commodities whose merits are already well known may be had at a given store for a price lower than the usual one. Commodities so advertised are called "leaders." Leaders to be effective must be articles in popular use; they must be readily identifiable, and of well-known quality; and lastly, they must be known as "standard price" goods, that is, goods which are customarily sold in all stores at one uniform price. The use of leaders constitutes a powerful advertising force in the retail trade. To be sure, the leader itself is sold generally at a loss. This sacrifice is usually rewarded, however, by an increase in the number of customers. The experienced dealer knows that a certain definite percentage of these customers will make other purchases upon which compensating profits may be realized. Hence he is unable to see that this type of advertising is essentially different from any other.[1] All advertising has for its purpose to attract trade. If price-cutting accomplishes this and increases sales to that point where all price-cutting losses are more than offset by consequent gains, then why is its use not economical? In the numerous cases where the dealer takes this position honestly, his motive may not properly be called predatory. There may be present a fault of judgment, but this does not mean viciousness of motive.

Additional justification for below-cost price-cutting frequently occurs. Seasonal changes often find the dealer with a stock of goods on his hands for which the active demand has disappeared. Similarly, changes in fashion will stigmatize his goods as being out of date. In such cases good business demands their sale even at heavy sacrifices. To carry them longer would only encumber his shelves, and tie up capital which would serve much better purposes elsewhere. If price-cutting will effect their riddance, its use is justifiable.

[1] *Hearings*, Jan. 5-11, pp. 195-200.

Again in cases of bankruptcy, or when a dealer is retiring from business, or entering a new line of business, or removing his business from some distant location, a quick liquidation of stock is generally necessary, and will justify price-cutting.

This outline of the different types of price-cutting shows that they may be based upon essentially different motives. Only in one type do we find the underlying motive open to the charge of being at all reprehensible, and even then it may be said to occur but rarely.

Further inquiry suggests not only a difference in underlying causes but a variation in results when the different types are used. That the extreme or below-cost type when used chronically and purely as an advertising device may be productive of evil to the trade and to the public seems well established. A hypothetical case will illustrate just what happens, according to the evidence of the manufacturers.

A druggist, John Doe, in a given town, cuts the price on a well-known safety razor and gives wide publicity to his act. Other druggests in this town also handle the " well-known " safety razor. But all future buyers of the article will satisfy their want at John Doe's. The other druggists are no longer able to sell their razors at the usual price. John Doe is using them as leaders, and he will continue to use them as such so long as the other stores maintain their prices. This action on their part would help him accomplish his purpose, namely, to attract to his store all buyers of the razor in question, and by implication to establish a reputation for cheap selling. This motive is recognized by the competing druggists and they lower their price to meet the John Doe price. This may be a below-cost price. If so, obviously a loss is entailed, heavy or light according to the number of razors in stock. Moreover, the greater part of the advertising advantage from the cut accrues to John

Doe. In the long run the cut will afford but little advertising value to *any of them.* A uniform cut-price on any given article in all the stores offers to the buying public no special incentive to favor any one store. The total demand distributes itself back to the original *status quo.* Eventually other cuts are made, and the entire process is repeated over again. Now for a summing-up of the results of this typical instance of price-cutting,[1] from the standpoint of the retailer.

John Doe has enjoyed at least a temporary advertising advantage. This perhaps outweighs the losses suffered from the cut-prices for the time being. Eventually, however, the advertising advantage disappears. But the cut-price remains, for it has been met by his competitors, and to attempt to raise it again would be folly. Hence, so long as he handles this good his loss from it must continue.

The other dealers are in yet worse plight. The original cut cost them an amount ranging, perhaps, from 10 per cent to 30 per cent of the value of their stock of razors. The subsequent continuance of the cut affects them just as it does John Doe. And in recompense they have enjoyed practically no advertising advantage from it.

In practically every large town there are many who practice price-cutting, and many are the goods that are cut. While druggist *A* is cutting on razors, druggist *B* is cutting on hair tonics; druggist *C* on soaps, and druggist *D* on tooth pastes. The same thing is being enacted among the grocers, the jewelers, the hardware merchants, and the dealers in dress goods and foot wear. The total results are the complex of what happened in the John Doe case. Each one strive to make a specialized appeal to the buying public. The efforts of one largely offset the efforts of the other.

[1] *Harper's Weekly*, Nov. 15, 1913; "The Competition that Kills" by Louis Brandeis.

On the goods cut all may eventually suffer losses.[1] And finally, the total public demand has not been permanently and generally increased. The temporary enlargement, if one occurs, soon gives way to a rapid diminution.

What, then, must be the attitude of the retailer towards goods whose prices have been cut below the profit-yielding point? It is asserted that they can no longer be of any great value to him. If he continues to carry them at all, it is for the purpose of maintaining variety of stock, or of accommodating those customers who have grown to like the commodities and persist in calling for them. This often happens in the case of widely advertised goods of especial merit. But the interest of the retailer in them is dead. He carries them reluctantly. If he can divert the demand for them to substitutes he generally does so.[2] When the dealers cease actively to push any given commodity the effect must be to diminish sales.[3]

The next distributive factor to be affected is the wholesaler, or jobber. Relying as he does directly upon the retailers, he suffers in common with them. Price-cutting reactions upon him are as pronounced as upon the retailer, both in manner and in degree.

Upon the manufacturer [4] more heavily than any one else fall the injuries resultant from price-cutting. It may be that his plant is highly specialized, and so capable of producing one type of commodity only. If so, his situation may be desperate. Should he be a producer of varied lines of goods, he may retrench losses on one by special attention to an-

[1] *Hearings before Int. & For. Com. Com.*, May 30 to June 1, 1916, pp. 4-46. Evidence of Dr. Paul Nystrom. *Hearings, ibid.*, Feb. 27, 1914 to Jan. 9, 1915, pp. 21-23. Testimony of Mr. Brandeis.

[2] *Hearings, op. cit.*, pp. 102-108.

[3] *Hearings, op. cit.*, pp. 72-85. Testimony of Dr. Lee Galloway.

[4] Address of W. H. Ingersoll before Nat'l Chamber of Commerce, Feb. 13, '14.

other. If his machinery is not too highly specialized, he may be able to save himself by producing an entirely new type of commodity. A mere change of brands may often be sufficient to curb the evil effects that react back upon him from the price-cutters, but this means a sacrifice of the good-will which has been built up about the old brand. Some loss he is bound to suffer, however, whether it be great or small, depending upon the degree, extent, and rapidity of the price-cutting, together with the degree of flexibility of his own enterprise. It is alleged by upholders of the price-maintenance principle that many establishments have been forced out of business through no other cause than their inability successfully to resist the price-cutters. It is difficult, indeed, to substantiate such allegations, however, for the failures in question may have been partly due to general inefficiency, and unwise business practices entirely apart from considerations of price maintenance. We, therefore, refrain from citing these specific instances. More in order is a submission of evidence from various manufacturers now doing business, and to whom the enquirer may turn for further substantiation.[1]

The manufacturers of rubber heels are constantly suffering losses from price-cutters. C. V. Engstrom & Co., manufacturers of Tred-Air, Essex, and Acme brands of rubber heels, state that they have often been compelled to sell goods at cost to meet the competition of price-cutters. The Foster Rubber Co. has been similarly affected.

A letter from the Ridgely Trimmer Co. contains the following:

One Spring we noticed our sales increasing terrifically, and we couldn't account for the cause, but it bobbed up serenely in all its glory a little later. The buying was done indirectly

[1] Letters submitted to the U. S. Chamber of Commerce by the manufacturers are the source of these specific instances.

for two catalog houses who came out with full page ads. cutting 25% from our regular resale price. . . . The result was a big outcry from the trade, and a falling off in sales. We have been practically two years getting back to where we were before that price cutting, and we are not back yet.

Houghton Mifflin & Co., publishers, complain that great havoc is being wrought in their book business by department store price-cutting.

The New York Wholesale Grocers' Association avers that Star Salmon, Star Lobster, and Burnham and Morrill's Corn, once popular brands, have been eliminated by price competition.

The National Hardware Association reports that the Gillette safety razor, previous to the recent court decisions, uniformly sold for $5.00. It was then universally handled. Prices are now being cut in many centers to as low as $2.50. Their cost to the retailer is $3.75. As a result other brands are now being pushed, displacing the Gillette.

The West Publishing Co. reports that on a certain expensive set of law books the prices were so seriously cut that they finally had to refuse to sell to dealers, and now sell to the lawyers direct.

The Mennen Chemical Co. quotes some instances where its products were heavily cut and, as a result, their business ruined in those centers.

The manufacturers of Lyon's Tooth Powder, according to their letter, have experienced a dropping-off in their sales along the Pacific Coast to the extent of at least 50 per cent of their former business, due to no other cause than price-cutting.

The Bon Ami Co. alleges that the Atlantic and Pacific Tea Co. has, by cutting the price of its product, greatly embarrassed its distribution.

Eberhard Faber Co., manufacturer of pencils, states as

follows: "The Mongol pencil is one of the most widely advertised, and probably one of the best known, pencils in the country. Because of the fact of price-cutting, we find that our sale for it has dropped off to possibly 25 per cent of what it used to be."

The Bissell Carpet Sweeper manufacturers reported that their business at one time was practically ruined by the price-cutters. Recently they have succeeded in restoring it by the active exercise of a price-maintenance policy.

Equally unfortunate were the effects upon the Waterbury Watch, as is indicated in the following quotations taken from the *Hearings of the Committee on the Judiciary* (1914), vol. 2, p. 1690, with respect to trust legislation:

Mr. Webb. What has become of the old Waterbury watch that we used to have as boys?

Mr. Ingersoll. That is in the graveyard of the price cutters. That watch was sold all over the country by every Tom, Dick, and Harry at any price that the dealer might take a notion to sell it at, and it went into the hands of a receiver because nobody would sell it. It came to be a stench in the nostrils of every decent, self-respecting merchant in the United States. The public was deprived of the privilege of purchasing the Waterbury watch from the time that the thing became so demoralized that nobody would handle it.

. . . Over here in Philadelphia there is one man selling our goods (the Ingersoll Dollar Watch) at 59c. The name of the concern is I. Press & Co., and they sell our watch at 59c. I do not know what they have to pay for them, but presumably they pay 67½ cents, 70 cents, or 72½ cents, because those are our prices. This dealer buys them from a wholesale dealer, and not from us. . . . In Philadelphia there are 14 dealers right close by this price cutter and another one named Kerstein. Now, I have some letters here bearing on this subject. Here is one from a man who says, "I cannot sell your goods at a profit any more. I used to buy them by the gross, but I can

no longer buy them by the dozen." Now Gentlemen, that is the way it affects us. The man who cuts the price down on articles like this does not want to sell them, and, under those conditions, nobody else can sell them. The result is that the public after a little while has great difficulty in getting those things.

Mr. Dyer. How does the sale of watches by your company now, under these conditions, compare with your sales prior to this decision by the Supreme Court which you spoke of? (Bauer *vs.* O'Donnell decision).

Mr. Ingersoll. That decision was handed down last May, and our sales for the first three months of this year, or just about up-to-date, as compared with the sales during the first three months of last year, are short in the neighborhood of 12%. We have suffered that loss, and it is mostly in the communities where this price cutting goes on.

The Kellogg Corn Flakes Co. has gone on record as being a great sufferer from price-cutting. To stifle it they have resorted to the courts numerous times.

The B. V. D. Co., manufacturers of underwear, have waged many bitter wars with the price-cutters, and experienced heavy losses in consequence.[1]

The above are typical of the complaints constantly being made by the manufacturers. Their number and tone carry conviction. But the assumption that these representations are wholly truthful leaves the case for price maintenance unproved. It will be noticed that in those instances where price-cutting has unquestionably injured the market, the effect has been brought about by price-cutting of the extreme type. Furthermore, large numbers of dealers irrespective of their costs of operation engaged in such price-cutting. Not price-cutting merely, but price-cutting run-

[1] *Hearings before the Committee on Interstate and Foreign Commerce* (House), Feb. 27, 1914 to Jan. 9, 1915, pp. 115-139. Evidence submitted by Mr. E. A. Whittier.

ning wild caused the evils. The goods lost favor with certain dealers because the profits from them disappeared. Disappearance of profits is not a necessary consequence of price-cutting, even though it occurs, under present conditions. In dealing with price-cutting two things of importance must be noted before indulging in conclusions: 1. the *degree* of the cut in price; 2. the class of dealers most affected by the cut.

Any given cut in the price of any commodity has a uniform effect only upon stores of the same general class. Stores of the same general class are similar as regards variety and size of stock, the class of people catered to, the degree of accommodation rendered to customers, and the type of organization, *i. e.* whether mail-order house, chain store, department store, independent, general, or specialty. Close similarity in all four of these respects will engender the maximum degree of competition as between stores in a given community. As the degree of similarity diminishes, the degree of competition also diminishes. The price policies of a large department store need not seriously concern the manager of a small specialty store, even though the latter be located on the neighboring block. The chain store, with its cut prices but with no delivery or credit accommodations, is not necessarily a menace to the independent store which offers these accommodations. Many people prize credit, delivery, and telephone service more highly than they value cut prices. The store which makes a special appeal to the wealthier and more discriminating classes by creating an atmosphere of elegance and refinement, and by the utilization of an unusually varied and excellent stock can often afford to ignore the next-door neighbor which bases its appeal on price-cutting.

Many instances abound to confirm these propositions. It is a matter of common knowledge that in the shadow of the

great department stores are found numerous and prosperous specialty stores.[1] It is not unusual to find on the same city block two stores selling the same standardized, trademarked goods at appreciably different prices.[2] As likely as not the store with the higher prices will have the larger volume of business and the greater prosperity.[3] At this point we are not interested to know why these price differences fail to react injuriously on the parties involved. It is sufficient to know that under certain conditions these price differences do occur without bestowing upon the price-cutter special advantage or imposing upon the price-maintainer any particular handicap.

The advocates of price maintenance have failed to take these facts into consideration when making the usual general argument that price-cutting is contagious, means enforced losses to the dealers, and the partial if not complete disappearance of the product from the market. Even in the small towns where one would expect general uniformity of price schedules in connection with standardized goods, and hence disastrous results from price-cutting, there are generally found at least two classes of stores, which follow entirely different principles in their price-making.[4]

We are now in a better position to illustrate the reactions which occur when price-cutting is limited to the economically justified type. Assume that John Doe in this instance is a druggist of more than usual business ability. By the judicious buying of goods and selection of stock, by skilful window display, by attractive advertising, by wise pricing

[1] *Hearings before Int. & For. Commerce Com.* (House), Jan. 5-11, 1917, p. 117.

[2] *Hearings, ibid.*, p. 112.

[3] *Annals of American Academy of Political and Social Science*, March, 1919, p. 197.

[4] Bulletin of Harvard School of Business Administration on *The Retail Grocery Business.*

of his goods, by honesty and reliability in his business, by advantage in location, by the exercise of great prudence in giving credit accommodations, by the employ of well-trained, courteous salesmen, and other possible economies, he is able to reduce his costs of doing business to a point 8 per cent, or even 10 per cent, below the costs of the average druggist.[1] This saving in costs being realized, John Doe may do either of two things. He may take the increased profits which he has made, and be satisfied with them, or he may sacrifice these profits for the time being to his customers with the object in view of building up a larger clientele, and have a greater volume of sales. If he is a man of foresight, he will adopt the latter course, that is, cut prices on his goods in direct proportion to his decreased costs, and no more. In the absence of emergencies, he would not cut the price *of any article below a profit-yielding point.* The result now would be that every retail druggist in the radius of his influence would be compelled to meet his cuts. To the less efficient ones this might mean a loss of profits on certain goods and the discontinuance of their sale. But John Doe still carries the goods, makes a profit on them, and is glad to accommodate all who desire the article. Consumers will be benefited by the situation. No harm need accrue to the manufacturers or the jobbers. Though the number of their distributors has been decreased, their volume of sales has not necessarily diminished. In fact, the chances are that the sales would be markedly increased by reason of the lowered price.[2] Moreover, the sum total of the costs of distribution would probably be less. In such an ideal situation every factor in the distributive system would be the gainer, the consumers

[1] See report of the Straus-Brown joint debate before Trenton Chamber of Commerce, Apr. 11, 1916.

[2] *Hearings before Int. and For. Commerce Committee*, Jan. 5-11, 1917, pp. 197, *et seq.*

would be benefited by lower prices, and nobody need be injured but the hopelessly inefficient retailer.[1] For this no lamentations should be made. The passing of the economically inefficient, as a result of the pressure of fair competition, is a thing to be desired. Though such a situation as is here chosen is an ideal one, its approximate realization is by no means impossible. At present, it would not work out as described, mainly because of two reasons: (1) Retailers now have the power of *unlimited price-cutting.* (2) The peculiar conditions in the retailing field would make the exercise of this unlimited power almost inevitable. Hence, any move to cut prices, howsoever justified by economies and honesty of motive, serves as an impetus to others to cut prices.

By way of illustration, the following instance will serve. The quotation is from the testimony of Mr. Erlanger, president of the B. V. D. Co.

On May 9th, 1913, a Boston retailer wrote us, complaining of the action of a competitor in cutting the price of our 50 cent article one cent. . . . Soon thereafter we had a telegram from a large dealer in Boston, complaining of a thirteen cent cut on the same article on the part of a competitor. . . . This dealer did not want to cut, but felt that he had to do so to compete. On the same day we had another telegram from another Boston dealer complaining of the action of both of these houses in selling our fifty cent goods at thirty-seven cents. In other words one dealer in Boston, by starting the cutting, precipitated a warfare which injured them all, as well as hurt-

[1] With respect to the effects of price cutting on advertised goods, Mr. Raymond S. Callahan of New York University, as a result of a personal investigation upon which he based a Master's dissertation, draws the conclusion that a lowering of price on a standard-price commodity does not tend to lower it in the estimation of the buying public. (See other allusions to this in *Hearings before the Interstate and Foreign Commerce Committee*, Jan. 5-11, 1917, p. 139.)

ing their neighboring dealers, and which, it is safe to assume, did the public no good, inasmuch as they made up their profit on other goods. The strife went further and before it finished extended largely throughout New England. I have computed that one of the dealers, in a single day in this strife, in selling 3600 of these fifty cent garments at twenty-seven cents each, and twelve hundred of the dollar garments at fifty-five cents each, lost seven hundred dollars, recognizing 25% as his expense.[1]

Instances of this sort which seem to indicate that price-cutting is necessarily contagious have caused the manufacturers to oppose all price-cutting regardless of degree or justification. More reasonable would be opposition only to that type which is really injurious. But presentation of this argument usually elicits from the advocates of price maintenance the objection that the distinctions made are of small importance. They maintain, as a rule, that such differences as exist among dealers with reference to operating costs and amounts of service granted to consumers are not sufficiently weighty to justify variations in the retail price. This objection calls for the chapter which follows.

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Those opposed to price maintenance. *Hearings before Int. & For. Com. Com.*, Jan. 5-11, 1917, pp. 4-35, 38-78, 79-80, 159-169, 197-199, 203, 207, 210, 211-215, 265, 287, 438, 476-483, 640, 645; *American Economic Review*, March, 1916; Article on "Price Maintenance," by F. W. Taussig.

[1] *Hearings before the Committee on the Judiciary* (House), 1914.

CHAPTER IV

The Irregularities of the Present Retailing System

Of the different types of retailers let us first consider the chains. The growth of the chain stores has been phenomenal. There are now in the country about 2000 chains comprising approximately 25,000 stores. They occupy every branch of the retail trade, though the grocery business claims the largest number of them. Hurd and Zimmerman (in *Printer's Ink*) estimate that there are 500 grocery chains, and that they do 5% of the total grocery business. Cities alone considered, they perhaps do at least 25% of the grocery retailing. Their most striking development is to be seen in Philadelphia, where they do over 60% of the grocery business and control over 1200 stores.

The largest of the grocery chains is the Great Atlantic & Pacific Tea Co. with 2,339 stores in 1916, and a capitalization of about $2,100,000. One of the most aggressive of the grocery chains is the Kroger Grocery and Baking Co. of Cincinnati, which in 1914 did a business totaling over $10,000,000. The Bowers chain in Memphis is also noteworthy in its growth and methods. The James Butler chain has over 200 branches, and is thriving on a capitalization of ten million. The Acme Tea Company, with over 300 stores, is one of the largest of the Philadelphia chains, and has branches extending throughout New Jersey.

Other representative grocery chains are the:

Name of chain	*Number of stores*
Grand Union Tea Co., Brooklyn	200
Wm. Butler, Philadelphia	140
O'Keefe, Mass.	146
Robinson & Crawford, Phila.	129
J. T. Connor, Boston	110
J. G. McCrory	115
The Childs Co., New Jersey	225
J. Belle Co., Phila.	130
J. P. Thompson Co.	73
G. M. Dunlop Co., Phila.	106
The Mohican Co.	50
G. S. Kresge Co.	124 [1]

In the drug field there are about two hundred chains. The largest of them is the new Liggett's-Riker-Hegeman combination, controlling approximately 200 stores. The Owl Drug Co. is a chain operating on the Pacific Coast, consisting in 1914 of 20 stores, and having a capitalization of 6½ million. A most striking development in the drug business is the United Drug Co. It has a capitalization of over 20 millions, and agencies to the number of 7000 in 1916. They compose the famous Rexall Group, and are the exclusive agents for the Rexall goods. The chain is unique in that the central organization does not own the agencies. The agencies become such in virtue of their capacity as stockholders in the central organization. To qualify for an agency one must become a stockholder. In this way the allegiance and interest of the distributors are closely held, the prices of the goods are maintained, and profits are shared in equal proportion by all. No more splendid example of effective and durable co-operation, in both producing and selling, is to be found anywhere. Notable also is the American Druggists' Syndicate formed by an association of about 16,000 retail drug stores. It is

[1] A series of articles in *Printer's Ink*, 1914, by Hurd and Zimmerman.

essentially co-operative both in buying and selling, and also engages to a large extent in manufacturing (1916).

In the retail tobacco business there are from 250 to 300 chains, aggregating over 2,500 stores. The largest and best known of these is the United Cigar Stores Co. In the late nineties it had its beginning in a very small way in Syracuse, New York. Later it became a subsidiary of the American Tobacco Co., but the Supreme Court, in its American Tobacco dissolution decree of 1911, forced it back into the independent state. It has grown with amazing rapidity, until now it has branches in all the larger cities of the East. Its capital is $35,000,000, and its one thousand stores did in 1913 a business of 32 million dollars.

That wonderful type of retailing establishment known as the "5 and 10" is not to be outdone in the formation of chains. There are about 180 chains of such stores comprising 2000 or more branches. The Woolworth chain, of whose success New York's mightiest skyscraper furnishes ample evidence, is the largest of them, with 805 stores in 1916, and an annual business of over $87,000,000.

There are about 100 restaurant chains, with 1400 branches. Typical representatives are the Baltimore, and Childs systems, familiar to all the cities of the East.

In the retailing of men's clothing, something like 45 or 50 chains are engaged, comprising over 600 stores.

The jewelers also have become a part of the chain movement, having at present about 50 chains. A new development is the "United Jewelers," which is constructed along the same lines as the United Drug Co. In 1914 it had 287 branches. Their avowed purpose is to absorb the better class of jewelers, not only to secure better price protection, but to push a common brand—the Hallmark brand.

In the meat business, the chains number about 75 with 450 stores, the largest chain being that of Oppenheimer, who has 32 separate establishments.

In the dairy field there are 40 chains. The Slawson-Decker chain has 83 establishments; Borden Condensed, 77; Nelson of New Orleans, 27, and Hood of Boston, 20.

This indication of the extent of chain-store development, brief and incomplete though it is, yet establishes fully that no program of price control can safely be advanced which does not give due consideration to this new and powerful factor in the distributive system.

Hardly less striking than the rapid growth of the chains has been the development of the department stores.[1] They are to be found in all the large towns and cities of the country.[2] Exact figures as to their number, and the percentage of the country's business which they do, are not available, but that they constitute an extremely important division of the retailing business is evident. Not content with their power as individual establishments, which in many instances is enormous, they are gradually combining themselves into chains. There are now numerous department-store chains, of which the Claflin Chain, and the May Chain are familiar examples.

Closely approximating the chains and department stores in importance are the mail-order houses.[3] It is difficult to estimate the amount of business being done by this type of retailer, as the mail-order business is carried on by a great number of establishments which are classified as department or general stores. In fact, practically all department stores have their mail-order departments, through which they serve their out-of-town customers. Of the strictly mail-order houses, Professor Nystrom estimates [4] the number to

[1] Address of W. H. Ingersoll before National Civic Federation, Dec. 12, 1913.

[2] P. T. Cherington, *The Advertising Book*, ch. vi.

[3] *Ibid.*

[4] Nystrom, *Ec. of Retailing*, ch. xiv.

be 1200, with an aggregate business of over $500,000,000. The principal mail-order houses and their annual business are as follows (1914) : [1]

Name of company	*Annual business*
Sears Roebuck & Co.	$90,000.000
Montgomery Ward & Co.	50,000,000
John M. Smyth	7,000,000
Harris Brothers	5,000,000
Chicago Mail Order House	5,000,000
Spiegel, May, Stern, Co.	5,000,000
Boston Store	2,000,000
National Cloak and Suit Co.	15,000,000

The business seems to yield exceptionally high profits. Sears & Roebuck paid dividends of about 23% on its common stock in 1914. In 1915 it paid a 50% common stock dividend. Montgomery Ward seems to be enjoying almost as high a degree of prosperity, and reports from the National Cloak & Suit Co. are remarkably glowing. The balance-sheet of Sears, Roebuck & Co. does not show gross profits, but Professor Nystrom from the other data given estimates that they amount to about 54%. Estimates as to their cost of doing business vary from 16% to 23%, about the same as the costs of the average small dealer.[2] Their percentage of profit, however, is immensely larger. It follows that they are either buying at lower prices than the average retailer can command or they are making more rapid turnovers than the average retailers, or both. As a matter of fact, the last situation is the true one, and it is true not only of the mail-order houses, but also of the chains and department stores.

The cost of operation of the department store is relatively higher than the mail-order house, and is generally

[1] Nystrom, *Economics of Retailing*, ch. xiv.

[2] Butler, *Marketing Methods*, pp. 107-120.

estimated to be about 30%. This in reality is not so high as it appears when we consider that it includes the cost of the wholesaling functions, as well as the ordinary retailing costs. Furthermore, it must be kept in mind that the percentage of operating costs is figured on the basis of net sales, and hence is necessarily no index to profits, as it does not indicate the tremendous discounts and rebates which department stores can command in their purchases.

Chain-store costs are much lower than those of department stores, and average, perhaps, not more than 16%. The United Cigar Stores claim to have an operating cost of only 10%. The reason for this becomes apparent when we consider that this chain has developed a remarkable rapidity of turn-over; it claims an average of 50 turn-overs annually.[1]

Rapidity of turnover is a goal for which all these big types of business are striving. A margin of profit per turnover that would mean starvation for the smaller dealer will net to them in the long run handsome profits, owing, of course, to the sheer number of turn-overs.

But the all-important question to be decided is: do these big retailers owe their rapid growth to fair and legitimate business practices, and, if so, are they able to offer to the public substantial price reductions based on genuine economies? Manifestly, if this question can be answered in the affirmative, the allegation that the chain is a menace to the individual retailer, and hence should be checked by an enforced price-maintenance policy, ceases to be convincing.[2]

Perhaps the most comprehensive study of the operating costs of the small retailer is that one made by the Harvard School of Business Administration. Their inquiry was

[1] *Printer's Ink*, Dec. 3, 1914 and Dec. 17, 1914.

[2] *Journal of Commerce*, March 13, 1916, p. 13. Article by T. F. Whitmarsh. Also Butler, *Marketing Methods*, chs. vi and vii.

confined, however, to the grocery business. Full reports, tabulated on standard forms, were secured from 253 retail grocers doing business in both large and small towns in the Middle West. These reports indicate that retail grocers do business at an average cost of 16.5% of net sales, and that their net profits vary from 2½ to 5½%. The standard of deviation for the cost figures was rather high, the figures ranging from 10.4% to 25.2%. The average gross profit, that is, the difference between net sales and the cost of their stock, was found to be 21%. The variation is from 14.6% to 28%.

Other facts were discovered which are of value to us. The following are some of them. In the retail grocery trade there are several classes of stores. In each town there is usually at least one large store which sells fancy groceries and specialties. The margin of profit and the expenses of such stores are usually higher than in other stores; the service requirements are greater.

It is of unusual interest to learn that, "The lowest expense ratios were not found in the largest stores, nor the highest in the smallest stores. The greatest variations were commonly between stores of approximately the same size operating under similar conditions in a single locality. As a general rule the common figures for the stores in one city correspond closely to the common figures for similar stores in other cities."

The element of variation in cost is the point here to emphasize. We read further in the report: "The common figure for rent expense in retail shoe stores is 5%; in retail grocery stores it is 1.3%, varying from 0.3% to 4.1%. In grocery stores the tendency is for rent to be less than 1.3% rather than more, and a significant number of stores have a rent percentage of less than one per cent."

"Net profit figures vary very widely, as above indicated. In fact, several stores have proved to be operating at a net loss when the proprietor's salary and other items were properly charged as expense."

The proportion of sales-force expense differs widely as between different stores. "It can be stated conservatively that in retail grocery stores the average sales per sales person range from $5,000 to $20,000 per year." It is not surprising, then, that the percentage figures of sales-force expense vary from 3.5% to 10.6% of net sales.[1]

From this report on grocery costs we desire to draw special attention to these points: (1) That the costs of doing business vary widely—from 10% to 26%. This great variation is made still greater, if we bring into consideration chains and department stores—from *10 per cent to 30 per cent.* (2) That these variations seem to occur irrespective of place or volume. (3) That there are to be found great differences as to the variety of stock and the amount of service accommodations in the various stores considered.

Therefore we must deduce the conclusion that for every store there is a composite of conditions peculiarly its own.[2]

[1] *Cf.* Nystrom, *Retail Store Management,* ch. vi.

[2] A survey by the Curtis Publishing Co. relative to the costs of doing business throughout the country brought to light the following conclusions:

"The cost of doing business varies in different parts of the country, in different cities in different parts of the country, in the same cities in different parts of the country, and the cost of doing business varies in cities of different size in the same part of the country. In rural stores the cost of doing business ranges from 10% to 20% in the East; from 11% to 20% in the middle West and South, and from 15% to 25% in the far West and mountain states.

"In towns of from 2000 to 10,000 the range of the cost of doing business is from 17% to 23% in the East, 18% to 21% in the middle West and South, and from 20% to 27% in the far West. In cities from 10,000 to 200,000 the cost of doing business ranges from 20% to

This applies in a somewhat less degree to other classes of retailers, the principal difference being that the costs of operating are uniformly higher among other retailers, especially those in the drug and clothing business—a difference due chiefly to their more pretentious requirements as to floor space, service and location. But the fact remains that, as between retailers of any given type of goods, there are to be found the same variations in the cost of doing business as are found among grocers.[1] We should expect

25% in the East, 20% to 26% in the middle West and South, and 25% to 32% in the far West.

"In cities from 200,000 to 600,000 the cost of doing business ranges from 22% to 27% in the East, 23% to 28% in the middle West and South, and from 28% to 34% in the far Western states. In cities from 600,000 up the cost varies from 24% to 31%. *Hearings before the Interstate and Foreign Commerce Committee,* Jan. 5-11, 1917, p. 337.

[1] COSTS OF OPERATION IN SHOE STORES

Costs of those selling low-price shoes

Items	*Variations*		*Common*
Gross profit	18.3%	to 40.4%	25.7%
Total selling expense	7.7	18.68	11.1
Total general expense	13.3	33.3	20.5
Net profits	6.5 (loss)	18.5	5.2
Stock turnovers	.7	4.77	1.6
Costs and turnovers of those selling medium-price shoes			
Gross profits	14.23	to 42.8	26.6
Total expense	13.3	34.66	20.25
Stock turns (absolute numbers)	.7	5.1	1.7
High-price shoes			
Gross profits	21.3	to 41.5	34.8
Total expense	23.43	32.85	28.8
Stock turns (ab. num.)	.92	2.33	1.5

COSTS OF OPERATION IN WHOLESALE GROCERY BUSINESS

Gross profits	7.7	to 17.2	12.
Total expense	6.7	13.74	9.5

(From bulletins 9 and 10 of the Harvard Graduate School of Business Administration, July, 1917, Feb., 1918.)

Dr. Paul Nystrom, one of the best authorities on the economics of

these variations to accord with differences in the amount of service rendered customers, or in the rapidity of turnovers, or in rent and wages. Such expectations are not freely met, however, because the factor of general business inefficiency plays too large a rôle.

There is no doubt, then, that a great part of the cost of operating, with respect to the average retailers, is but the cost of inefficiency.

Here we are forced to ask, can a system so rugged on its surface, so individualistic in its workings, form the basis upon which can be superposed a structure which is essentially uniform and rigid? Can the manifold conditions existent in the retailing field be reconciled to a price policy which is fixed and unchangeable? Can there logically or justly be imposed upon the individual retailer a given price for his every branded good to which he must conform, regardless of his efficiency, his selling skill, his economies, his service to the public?

But let us reserve the answer. Those same conditions among retailers which suggested the above questions are, no doubt, a partial explanation of the great growth of the chains. To the chains must be yielded this praise, that largely to them is due the introduction of scientific selling.[1] In the days when only the small-sized independent inhabited the retailing world, selling in many cases had become an art perhaps; but not until the appearance of the bigger

retailing, says on the subject of costs that in grocery stores the variation is from 12% to 22%; in dry goods stores the variation is from 16% to 25%; in furniture stores from 22% to 28%; in shoe stores from 16% to 27%; in hardware stores from 17% to 26%; in men's clothing stores from 20% to 30%; in drug stores from 24% to 30%; in jewelry stores from 25% to 32%; and in department stores from 22% to 30%. (*Hearings before the Interstate and Foreign Commerce Committee*, Jan. 5 to 11, 1917, p. 115.)

[1] *Printer's Ink*, Dec. 3, 1914. Article by Hurd and Zimmerman.

forms of retailing establishments, did it become to any great extent a *science*. The sales policy of every branch in a chain system is determined by the central management. Perfect organization is evident everywhere. The highest trained and most resourceful brains that large capital can buy are at the disposal of the chains. Every branch is continually under the most minute scrutiny and no efforts are spared to make it conform to the exact requirements of its own specific environment.[1] Accurate daily, and sometimes more frequent, accounting is required, detailed reports in nearly all cases being sent daily to the main office. All salesmen are trained to a uniform standard of selling methods. Benefits of experience gained in one store are applied to all stores. Great care is exercised in window displays, in bargain offerings, in advertising. Idle stock is never tolerated. Over-stocking is carefully avoided. Records are kept to the needs and demands of the community. Possibilities of future sales are never based on guess-work or hope. They are mathematically calculated. New branches are not installed until, by very close investigation, which sometimes goes so far as to count the people who daily pass the prospective site, the desirability of the location is well established. The salesmen are coached to avoid all waste and exert every effort to prevent the small leakages that in most stores are continually draining off profits.[2]

But this scientific selling, accounting, and conservation do not form the only device upon which the chains rely. Some of them, as the United Cigar Stores, Liggett's-Riker-Hegeman, and others, have become corporations, and issued large amounts of stocks and bonds in which the public is encouraged to invest. This not only results in the enjoyment of the usual corporate advantages, but is the instru-

[1] *Printer's Ink*, Dec. 17, 1915.

[2] *System*, May, 1916, "The United Cigar Stores Methods."

ment of most excellent advertising, and no doubt secures many loyal customers.

The chains, department stores, and mail-order houses are also superior in their buying advantages. Large capital enables them to derive the maximum benefits of the quantity and cash discount. Their enormous purchases make them the favored customers of the manufacturer. Instances are numerous where the manufacturer has actually sold to them at cost, in order to keep his mill at full running capacity, depending for profits on the smaller sales. President Miller of the Owl drug chain says that sometimes discounts are forced upon them by the manufacturer.[1] Some manufacturers, however, are strongly averse to the giving of discounts, on the ground that it stimulates price-cutting. Of these, J. H. Kellogg, and Wm. H. Ingersoll are well-known representatives.

Another development which has received marked attention from the big retailers, and to a less extent from the small ones, is the appearance of the so-called "private brand," that is, the brand of the dealer himself, as distinct from the manufacturer's brand.[2] Practically all of the large chains have their private brands. This is significant as showing a pronounced willingness on the part of the retailer to assume all responsibility for the goods which he handles. It must be admitted, however, that to a certain extent he has been forced into this responsibility by the habit of price-cutting. No more effective scheme for the indirect eradication of the price-cutters could be devised than a universal use of the private brand. For the retailers could sell goods of their own brand at whatsoever price they pleased, and the reactions therefrom would extend no

[1] *Printer's Ink*, Nov. 19, 1914 and Dec. 24, 1914.

[2] *Advertising and Selling*, Jan., 1915, "The Private Brand," by Zimmerman.

further than their own doors. The goods of other retailers, though similar in kind, would yet be firmly entrenched behind altogether different brands, and hence proof against injury resulting from price-cutting. The manufacturer would not be affected, for to all intents and purposes he would no longer be a factor in the distributive system. His function would be confined merely to manufacturing and packing, according to the order of the dealer. He would be responsible only to the dealer. The public would never hear of him, although the article which he manufactured might come before them disguised by a hundred different brands.[1]

In the path of the private brand there are, however, many obstacles. It could never be feasible in connection with the sale of certain specialties which have properties so individualistic and distinctive as to be readily identifiable by the public, regardless of brand. Nor would it be feasible in the distribution of patented or copyrighted articles. Furthermore, the private brand, except for the largest retailers, could never be a strictly economical device, for the same reason that an article "made to order" can never be quite so cheap as one "ready made" taken from stock. The proprietor of the brand, unless his sales are very large. would necessarily have to order his goods in limited quantities, thus entailing a larger cost per unit than he previously paid. This cost would be added to by the necessity of having distinguishing wrappings or cartons, and perhaps unique form or quality of goods. Ordering in large quantities would entail the investment of capital which for a long time would have to lie idle. Additional stock-rooms and warehouses would be needed. Furthermore, there would always be present the danger of quality deterioration, and

[1] *Journal of Commerce*, Dec. 6, 1915, p. 14, "The Manufacturer's Peril in Packing Jobbers' Brands;" Butler, *Marketing Methods*, ch. xiii.

possible losses from fire or a downward trend of the market. In many cases the maintenance of a special laboratory would be required.

Certain of these disadvantages are overcome by the actions of the manufacturing jobbers, who buy the goods in large quantities and equip them with the necessary wrappings or cartons before distribution to the retailer. Mr. Zimmerman describes it as follows: "They (the jobbers) put up brands as substitutes for all well-known products and afford the dealer opportunity to put them on the market in his own name. They give him plenty of credit, and offer him large profits. For instance, there is a certain tooth-paste put up by the jobber which is sold to the retailer at such a price as to allow him a profit of $1.80 per dozen, whereas the greatest profit he can make on a well-known brand is 60 cents. It costs him $1.20 per dozen. He gets 25 cents a tube, or three dollars a dozen, for it, and he knows that the customer cannot say to him, 'I can get it at Blank's for 15 cents.' This is one of the great features of the private brand. The retailer feels that he is building up an individual business of his own, that his preparation can only be obtained at *his* store. The dealer today who is compelled to feature a private brand uses the utmost care to make it stand the acid test of quality, for he realizes the value of the satisfied customer. Many dealers have made great progress with their private brands."

This specific instance taken in connection with Mr. Zimmerman's argument may seem quite puzzling to the reader. For although the dealer in question was making a gross profit of 166% on the private brand mentioned, he is spoken of as being "compelled to feature a private brand," and one wonders how it is possible that dealers have come to accept such handsome profits only under compulsion. The mystery will be cleared up when we consider that large

profit per unit does not necessarily mean large net profit. In retailing there are no large net profits without large volume of sales. One great difficulty with the private brand from the standpoint of the average retailer is the difficulty of obtaining this much-to-be-desired volume. The dealer no longer has the benefit of national advertising, nor help from the manufacturer in local advertising. He must rely upon his own efforts alone to build up his demand. If his store already has an established reputation for honesty and good values, his task, though simplified, is still difficult enough. For even with much capital at his disposal, how can he afford to advertise each specific brand? Probably from not one single brand could he expect a volume of sales sufficient to justify special advertising. How different is his position from the manufacturer's, who, having the whole country before him as a market, can afford to expend tremendous sums in advertising even the most trifling articles. For instance, Wrigley spends hundreds of thousands annually advertising his gum which sells for only five cents a package. Fancy the average retailer with his one or two jars of gum expending anything in advertising the brand he carries. "The live and aggressive dealer of today sees no intrinsic advantages in substitution. In fact, he sees great advantages in pushing the national brands, because they necessitate less time in serving the customer—mean more sales and more rapid turn-over. Even though he is working on a smaller margin of profit, he now realizes that if he can turn over a well-known brand ten or twelve times a year at a net profit of 2%, he will make more money than by turning over his private brand once or twice a year at a net profit of 8% or 10% each time." [1] Thus from an economic point of view the feasibility of the private brand,

[1] Zimmerman, "The Private Brand," *Advertising and Selling*, Dec., 1914.

with respect to the small independent retailers, is still much to be doubted. As a device for the chains and department stores and mail-order houses it is rapidly growing in favor, and seems to be free from those disadvantages arising from its use by the small retailers.[1]

The great outcry from the small retailers of the country against the tactics and growth of the larger retailing systems has served to draw considerable attention to the methods and tactics of the former as well as of the latter. That the small retailers have suffered to such an extent as actually to decrease their number seems doubtful. To be sure, in certain of the cities, as in Philadelphia, this has happened, but the instances are few. Furthermore, the dangers of such seem to be diminishing. The small independents are learning to meet successfully their larger foes, by the study and application of the methods of the latter.[2]

Formerly their inability to meet them could be attributed to the following reasons: (1) in what may be called "stock selection" the small retailers have often shown poor judgment. That is, they fail to measure correctly the community demand for certain commodities. They buy too little of one thing, too much of another. So pronounced has been this weakness that the manufacturers themselves, and the jobbers, have been compelled to restrict their sales in many instances, and to exercise organized efforts in educating retailers in the choice of stock. Over-stocking has been so prevalent that it has been asserted on good authority that 80% of the stock of the average retailer is practically dead—only an encumbrance on the shelves. This means that the retailers are having to live on only 20% of their

[1] Butler, *Marketing Methods*, ch. xiii, "The Private Brand Problem."

[2] *Journal of Commerce*, May 15, 1916, "The Future of the Retail Grocer," by John A. Green, Sec. Nat'l Retail Grocers' Ass'n.

stock, the part which is undergoing easy and rapid turn-over. From such a situation there evolves not only a serious loss to the merchant, but also a distinct disadvantage to the community as a whole, in that a large proportion of its purchases must be of goods old, stale, and otherwise deteriorated. (2) Not less prevalent than poor stock selection and over-stocking are unbusiness-like methods in accounting. Numberless merchants are totally ignorant as to the proper itemization of their receipts and costs. Often they deceive themselves into thinking their business is on a prosperous basis when as a matter of fact, they are losing money. The story is told of a merchant who after ten years of business decided to retire on his profits. The process of winding-up his affairs disclosed to him, however, to his great consternation, that he had no profits on which to retire, but was instead heavily in debt. There could possibly be no greater barrier to progress in retail merchandising than such self-deception in accounting. The truth of this is now being realized by many of the great manufacturers of the country, by the trade organizations, by business schools, and various government commissions. Consequently a campaign of education is being vigorously waged among retailers in the effort to establish universally more efficient systems of accounting. The success of this campaign more than that of any other will pave the way for numerous additional reforms in retailing which are now practically impossible. For instance, upon it will depend largely the eradication of such evils as injudicious pricing, extravagant buying, uneconomic service, wasteful advertising, excessive costs of operation—in short, the causes of the thousand and one leakages that perpetually draw upon the profits of the merchant. (3) Poor salesmanship may be said to be another of the retailer's cardinal shortcomings. Too many of them believed in the saying: "Anybody can

keep store." Slack attention to customers has resulted, poor display of goods, inadequate service, ineffective advertising. The windows are poorly trimmed, the show-cases slovenly kept, the floor and walls untidy, the atmosphere unattractive. The stores that come within this category—there are thousands of them, but they are getting fewer—cannot hope to compete with the modern Titans in the retailing world.[1] (4) Finally, there is to be noted what may be called the lack of business foresight on the part of so many small merchants. It is in reality a false sense of values. It expresses itself in the attempt merely to make daily profits, ignoring considerations of the future, of the needs of a growing community and of the social responsibility that may be involved even in retailing. In support of this, witness the hundreds of stores that, throughout the small towns of the country, have been slumbering for years, satisfied with the same limited and dingy quarters, the same old stock, the same old methods. How suddenly and rudely many of them are awakened by the incoming of the new competitor. The consequent stress invariably brings better retailing conditions, the merchants are stimulated to greater efforts, awakened to new possibilities, educated to a finer sensing of values in their business conduct.

Despite these shortcomings of the average retail dealer which have been outlined, he is destined to live—not only to live, but grow stronger and more efficient. He has been transformed by the new methods of retailing, methods which had their inception either in the big competitors or in the tremendous competitive pressure brought about by them. By way of illustration, witness the small retailers who are thriving within the very shadows of big department stores, and in close proximity to the most voracious

[1] *Printer's Ink*, Dec. 6, 1917, pp. 81-89; art. by P. F. Nowlan.

chains.[1] They have learned well their lesson in the newer efficiency, and have proved that the small store, when properly conducted, is a thoroughly efficient instrument for the distribution of goods to the ultimate consumer.[2] The following reasons may be advanced:

(1) The small store may be highly specialized with respect to the stock it carries. In this line the owner is an expert in buying, handling, and selling. A uniform turnover on all the stock is assured. No dead stock need burden the shelves. The expense of a varied stock is avoided.

(2) The personal element in service plays a large rôle. Usually the owner himself is present in the store. He should be able to make an appeal to his customers far more effective and lasting than that of the cheap clerk in the department store.

(3) Cost of operating is less in proportion to sales. The department stores as a rule strive to locate themselves in the most densely populated portions of the community—on sites where the rents are extremely high. The smaller store, on the other hand, may find a sufficient volume of trade for its needs in places where the rent is low. It pays less rent not only in actual outlay, but also relative to the amount of sales. The cost in rent for the average specialty store does not exceed one and one-half to two per cent of total sales. Rent for the large general or department store is frequently five per cent of total sales. The larger the sales, the larger the share the landlord seems able to exact. It is not unusual for the rent item to run as high as ten per cent of sales in the crowded central sections of the larger cities.[3]

[1] *Journal of Commerce*, March 13, 1916, article by J. S. Engart.

[2] *Ibid.*, Dec. 6, 1915, p. 13, "Is the Small Grocer Doomed?"

[3] Nystrom, *Economics of Retailing*, pp. 128-137.

Not only is a saving of rent effected, but also a saving from simplicity of organization. Departmental expenses are avoided, practically no clerical force is needed, newspaper and periodical advertising is not required, and practically no loss is entailed through the giving of credits, because such customers as are accorded credit are, as a rule, personally known to the proprietor. The delivery expenses of the neighborhood store, proportionally, are far less than those of the department store, owing to the limited territory to be covered, and to the large number of customers who act as their own carriers. The nearby residences of the customers make possible not only easy and speedy delivery, but in addition render practically impossible the loss of goods in transit.

Now if the above advantages are not offset by the disadvantages previously recounted, the welfare of the independent is in no imminent danger from the inroads of the larger competitors. The small retailers have only to look to their own efficiency for the most part.[1]

An additional weapon which the small retailers are using against the chains, department stores, and mail-order houses is the buying exchange. The purpose of this is to effect economies in buying by a general pooling of purchasing power. A central agency is maintained through which all the buying is done. The goods are laid down at the association warehouses, and from them are distributed by the retailers themselves at their own expense. As is apparent, the credit facilities of such an organization are extremely limited because of the very looseness and unreliability of the organization. The highest efficiency in handling and distributing cannot be expected. Nor are such organizations in high favor with the other factors in the distributive

[1] *Journal of Commerce*, March 13, 1916, p. 13, article by S. L. Stix.

system.[1] On the one hand they are fought by the jobbers, who perceive in them a serious menace to the present high state of the middleman. This hostility of the jobber is brought home to the buying associations by pressure exercised through the manufacturers. Manufacturers who heretofore have relied largely upon the jobbers for their distribution are loath to incur the enmity of the latter by meeting the requirements of an organization so undeveloped and so uncertain as the buying exchange. This truth has been clearly illustrated by the trade situation in Philadelphia. There, as has already been indicated, the chains have attained their highest development. So serious were their inroads that the independents were in danger of complete extirpation. Their number decreased about twenty-five per cent in five years, according to the estimate of the best available authorities.[2] Under the old business methods, the disappearance of the small retailer seemed but the matter of a short time. As a last resort the buying exchanges were instituted, the Philadelphia Association and the Frankford Exchange. Upon their inception, the jobbers became alarmed, and began to combat the exchanges by making alluring overtures to the yet independent retailers. The conflict became a triangular one, on one apex the chain stores, on another the exchanges, on the remaining one the independent retailers with their allies, the jobbers.[3]

The subsequent developments were interesting. The chain stores, feeling the pressure, began to seek for closer co-operation, forming a colossal chain of over 1200 stores. To meet this giant competitor, about 2500 of the independent retail grocers entered into a co-operative agreement with

[1] *Journal of Commerce*, Jan. 21, 1916. A discussion on chain stores and buying exchanges at Convention of N. Y. Wholesale Grocers Ass'n.

[2] *Printer's Ink*, Sept. 17, 1914.

[3] *Ibid.*, Oct. 25, 1917, pp. 37-40.

the Wholesale Grocers' Sales Co., designating themselves as the Community Stores. Each party to this agreement reserves perfect freedom of action, the purpose of the agreement being not to maintain prices or to restrict competition, but to secure concerted action in the marketing of goods. In accordance with a prearranged schedule, the jobbers purchase in conjunction certain stipulated brands of goods, the orders often, but not necessarily, being pooled. Then in unison the jobbers make their resale to the dealers, joining with the dealers in a great advertising drive which emphasizes only the goods in question and the fact that the goods are procurable at the Community Stores. This joint advertising by jobber and retailer is also supplemented, if possible, by the manufacurer himself.

The advantages of this scheme are: first, the jobbers realize savings from quantity buying in the usual way, and in addition are assured a rapid turnover of the specialized goods. Second, the retailers, all impartially designated as Community Stores, are enabled to pool the expenses of advertising and to enjoy in common the fruits thereof. Every advertisement is a thing aimed to secure the publicity of 2500 stores, and moreover it is paid for not by one store, but by 2500. Hence the average store receives more and better publicity than it otherwise would. Selling effort is more direct, more scientific, more purposeful, as within any given week every store is specializing in the sale of a particular line or lines of goods.[1]

The Philadelphia experiment, although encouraging to the advocates of buying exchanges and co-operative associations of retailers, is yet too local and too youthful to warrant highly optimistic conclusions.

[1] See *Journal of Commerce*, Jan. 2, 1918; articles by James Hewitt, Pres. of Penn., N. Jersey, and Del. Wholesale Grocers Ass'n; and Arthur Unger, Pres. of Phila. Ass'n of M'f'rs Representatives.

Taken as a whole, the buying-exchange movement has not been a very successful one. It is a thing apparently never resorted to except under great pressure. Even then its career is uncertain and its advantages doubtful. It undoubtedly does possess possibilities, however, which have not yet been developed through lack of effective organization, and co-operative spirit among the members.

The last type of retailing to be considered is that of the manufacturers' chain. In late years a number of these chains have been instituted. They at present constitute one of the very few ways by which the manufacturer may directly control his resale prices. In the boot and shoe industry such chains are familiar. It embraces, perhaps, fifty of them. The Walkover Shoe Co. has about 3500 agencies, not all of them exclusive, however; the Regal Co. has 1500, forty-seven of them being for its exclusive use. The Douglas, Florsheim, and Sorosis brands are also widely sold through such means.

Manufacturers of musical instruments often have their exclusive agencies, as, for example, the Steinway Co. with 28 stores; the Starr Piano Co. with 36 stores; the Baldwin Co. with 8; Conway with 10; Cable with 9; Kimble with 17.

The same is true of the makers of typewriters, the Remington Co. having over 200 stores; the Underwood Co. 220.

This has also been a favorite method with automobile manufacturers. Practically every large town has its exclusive automobile agencies, and this is no less true of certain clothing, and hat manufacturers; manufacturers of talking machines; sporting goods, etc.[1]

The movement on the part of manufacturers thus to effect their own retailing has been attributed by many to a desire on the part of the manufacturers to escape the price-cutters. Some profess to see in it a very dangerous ten-

[1] *Printer's Ink*, Oct. 22, 1914.

dency. If persistently followed, they say it will result eventually in depriving the regular retailers of the means of doing business, and furthermore, make of the manufacturer an absolute monopolist, as respects not only the manufacture, but also the sale of the specialty. It hardly seems possible, however, that the movement can extend over a great variety of commodities. In order for a store which sells only one commodity or one class of commodities to succeed, either the per-unit value of each commodity must be fairly high or else the demand must be wide and constant. These limitations will either confine the exclusive manufacturer's agency to comparatively high-priced commodities, mostly those in the luxury class, or else restrict it to the large cities only, where the demand would be large and uniform.

Thus, even though the growth of the manufacturer's chain may perchance be due partly to price-cutting, it is seriously to be doubted if any objection can successfully be raised against this method of retailing.

Additional References

On wholesalers: Butler, *Marketing Methods*, pp. 157-173; Cherington, *The Advertising Book*, ch. viii; Douglas, A. W., *Merchandising*.

On department stores: Nystrom, pp. 195-216; Butler, pp. 70-79; Cherington, *The Advertising Book*, ch. vi; *Hearings before Interstate and Foreign Commerce Committee of the House*, Feb. 27, 1914 to Jan. 9, 1915, pp. 88-108; Swinney, *Merchandising*, pp. 283-296.

On mail order houses: Butler, pp. 107-140; Nystrom, pp. 235-255; Swinney, *Merchandising*, pp. 319-330.

On chain stores: Cherington, ch. vii; Nystrom, pp. 216-235; Butler, pp. 79-105; Swinney, pp. 298-317.

On co-operative movements: Journal of Commerce, Oct. 18, 1915, p. 13, "The Philadelphia Jobbers;" *Printer's Ink*, June 6, 1918, pp. 26-31, "The Community Stores of Philadelphia;" Butler, *Marketing Methods*, ch. xiv.

On operating costs: Hearings before Interstate and Foreign Commerce Com., Jan. 5-11, 1917, pp. 79-80, 109, 112, 159-169, 343; Bulletins of Harvard School of Business Administration, nos. 1 to 10; Nystrom, *Economics of Retailing*, pp. 69-82, 172-195.

CHAPTER V

Price Control and its Relation to Quality and Service

If the dominant voice in the solution of the price-maintenance problem belongs to the consumer, no doubt remains that the moving considerations will be those involving

(1) Quality and service, with respect to the commodity.[1]
(2) Cost of living, or the price effects.

It is claimed by the advocates of price maintenance that its adoption would make for advantages in the form of superior quality goods, and superior service in buying. The first advantage will result from general improvements in the condition of manufacture.

To-day the sort of manufacturing that pays is generally the sort that requires a large capital outlay. Magnitude of capital is necessitated (1) by the requirements of large-scale production. This means not only the employment of much machinery and floor space, but a high-class and expensive administrative force adequate to cope with modern industrial conditions. (2) by the requirements of large-scale distribution. If a wide market is to be obtained for the goods, extensive advertising campaigns must be resorted to. Many and varied are the forms of advertising: magazine and newspaper advertising, bill-board advertising, mail advertising, *i. e.*, sending circular matter direct to the pros-

[1] *Rep't of the Nat'l Chamber of Commerce on Price Maintenance.*

pective consumer through the mails, and window-display advertising. The premium plan of advertising may also be utilized; but whatever the form, to be effective, it must be widespread, attractive, and continuous. Often it comes to be the most expensive single item in the cost of production and distribution. Many firms spend hundreds of thousands annually on magazine advertising alone.[1] Regardless of the economic advisability of such heavy advertising, it yet remains true that to a large extent present competitive conditions make it essential to the securing and retention of a wide market. It is asserted that heavy advertising expense will not be incurred unless the advertisers have a large degree of confidence in the success of their goods. The same may be said of expenditures sunk in machinery and other productive material. Whatever makes for confidence on the part of the manufacturer is an incentive to greater money expenditure in production. As such a creator of confidence, price maintenance serves excellently. Given a new commodity, which by local tests has proved itself acceptable to the consumer, an experienced salesman can with a great degree of certainty calculate the volume of sales which a certain sort and quantity of advertising will produce. But under the present system, possibilities of losses through the work of the price-cutter serve to discount greatly the value of any such calculations. As a result, the manufacturer must ever walk with halting steps, always more or less in a state of trepidation over fears of closed markets and hostile dealers.

It is asserted that this is a situation which not only endangers the life of the good, but seriously threatens its quality. If, through inability to protect his prices, the manufacturer is driven to the last ditch, his final form of

[1] *Journal of Commerce*, Dec. 6, 1915, p. 13, "Constructive Power of Good Advertising;" *Printer's Ink*, Dec. 6, 1917, p. 98.

defense must necessarily be in quality deterioration, or shortage in weight and measure. It is a matter of common knowledge that many well-known branded goods deteriorate in quality with the passing years. Also there are instances of short weight and measure, as recent investigations of the New York State inspectors have disclosed.[1]

But is this due to price-cutting? Other explanations have been offered. Increase in the costs of raw materials and labor, in the case of goods sold on a narrow margin of profit, undoubtedly has accounted for some of the complaints. Sometimes to make way for the promotion of new and more lucrative specialties, old brands are purposely made inferior. If their previous reputation has been good, all the better, for their selling momentum acquired through many years will keep them going well for astonishingly long periods, despite their recent inferiority, and to the great profit of the manufacturer. Again, many of the brands which to some are apparent victims of price-cutting, very probably were never meant for a permanent place in the market, but were brought into existence for "fighting purposes" only. The fighting brand is too well known to require further comment.[2]

Much plausibility seems to rest in still another explanation. After an article has been well established on the market for years, and people have reached the point where they buy it largely from habit, the manufacturer sometimes takes advantage of that trait in human nature called inertia gradually to lessen the quality or quantity of the good. From sheer force of habit people continue buying the goods, never noticing the deterioration, perhaps, until it has reached the extreme stage. Thus for a long time the manu-

[1] Superintendent of Weights and Measures of the State of New York, *Annual Report*, 1916, 1917.

[2] *Cf.* Stevens, *Unfair Competition*, Chicago, Univ. Press, 1917.

facturer may enjoy increased profits from such reprehensible devices before his sales begin appreciably to drop off.

So in many and various ways can be explained the tendency of goods to fall off in quantity and quality as the years progress. The explanation that it is caused by price-cutting is not an illogical one, but perhaps in no case is more than a partial explanation.

A far more virile argument is the one aimed at the private brand as a product of price-cutting. In a previous chapter it was indicated that to a certain extent the private brand was caused by price-cutting, especially so with respect to the smaller retailers. The economic aspects of the private brand were also mentioned.[1] At this point attention must be given to the quality and service aspects.[2] It is asserted by the proponents of price maintenance that goods nationally advertised, with standard trade-mark or brand, are as a rule manufactured with a large degree of publicity. The location of the factories is usually well known, and public interest in them is always alive. Moreover, they are easily subject to close investigation by health and insurance officers. Under such circumstances approved sanitary and labor conditions are always assured. For example, the nationally advertised cereals and the products of the National Biscuit Company are manufactured under conditions remarkable for their cleanliness and sanitation. The pure-food laws, the weight and measure laws, are complied with to the letter. It is to be doubted if such desirable conditions would generally prevail in the manufacture of private brands. Neither publicity nor the pride of proprietorship would have opportunity to manifest itself in securing cleanly and healthful working condi-

[1] *Cf. supra*, p. 59 *et seq.*

[2] *Hearings of Judiciary Com.*, p. 732. Statement of Mrs. Frederick (1914).

tions. The work of the state factory inspectors could never produce gratifying results. Their numbers and methods are too inadequate. In the production of the private brand, competition would thrive in its bitterest forms and be productive of labor evils, long hours, low wages, home work, and unsanitary conditions to an extent manifestly improbable in the larger and better known establishments.[1]

With respect to conditions of sale, the upholders of the maintained price assert that, in sales-making, quality should be considered above price, and to assure this primary quality consideration the fixed price is essential. If we accept the first proposition, the second follows as a matter of course, with respect to the majority of commodities. One of the most striking of recent developments in merchandising is the tendency of prices to vary in regular gradations.[2] It is sometimes termed price stratification, the thickness of the strata depending upon the value of the class of goods considered. For instance, most men unconsciously classify themselves as regards their shoe-buying habits. Before buying a shoe they have made up their minds as to the price they can afford to pay. Let us suppose now that a given individual has, in consideration of his past experience and present financial status, decided upon $5.00 as his price. His next act is to compare as actually as he can the many brands of shoe that sell for $5.00. The motive uppermost in his mind, now that the price decision has been made, is to secure the best possible quality. No longer does a man look around until he finds a pair of shoes that are apparently satisfactory, and then attempt by much argument and higgling to beat down the price of the seller. He has put

[1] *Printer's Ink*, Sept. 5, 1918, p. 97, *et seq.* "The Federal Trade Commission and the Private Brand."

[2] *Preliminary report of U. S. Chamber of Commerce Committee on Resale Price Maintenance.*

himself definitely in a price class, be it a $3.00, $4.00, $5.00 or $6.00 class. In the same way buyers may be classed as to the price they are willing to pay for suits of clothing. How many of us are there who do not, before entering a clothing store, make up our minds just what our price shall be? And the price we decide upon is not an odd one, but is generally one of a few well-recognized and popular, as $20.00, $25.00, $30.00 or $35.00, $40.00 or $45.00. By this habit we simplify our buying. It is a task purely of quality or pattern selection. Suppose that the principle of price maintenance were applied, say, to breakfast foods. Very probably the hundreds of brands of breakfast food, representing every possible kind and quality, would, so far as prices are concerned, be contained in no more than three price categories, 10, 15, and 25 cents-a-package categories. Obviously to average purchasers of breakfast food under such conditions no problem is presented, other than that of choice of quality as indicated by brand. One or another of the price categories is accepted and rarely departed from.

Such definite classifications, it is argued, not only are of aid to the consumer in buying, but vastly help the dealers in making their sales. Time is saved, as but little description or demonstration is required. All higgling as to price disappears. In short, it makes possible a maximum of efficiency in service. Upon the producer the effect is also salutary. Knowing that his brand has been definitely and unalterably, at least for a long period, classified as to price, his sole endeavor henceforth will be to provide for the price the best possible grade of commodity. Protected as he is in his price, he is no longer handicapped by having to cling always to a wide margin of safety with respect to his costs.

Advocates of price maintenance have gone so far as to assert that the general integrity of the nationally advertised trade-mark is threatened by price-cutting, that not only

does it cause occasional driving of goods from the market, and occasional quality deterioration, but it destroys the incentive that lies behind the promotion of specialties.[1] They strengthen this point (1) by demonstrating the advantage of the branded commodity from the consumer's point of view, and (2) by contrasting these advantages with the evils attendant upon the buying of goods in bulk.[2]

We must give full notice to these contentions, for they do affect vitally the point of view of the consumer. Upon his decision, as we have already intimated, must rest the ultimate fate of price maintenance. That system is to be preferred which is for the greater interest of the consumer —which assures him the greatest values for his money, and interweaves into market conditions forces that make for dependability, uniformity, and reasonableness. To emphasize the need for this, we here insert a paragraph from an investigation made by the New York Association for the Improvement of the Condition of the Poor:[3]

They were buying from the stores of a well known New York chain when they found that you could buy split peas for eight cents in two of the stores, which cost at wholesale 4.2 cents per pound, the profit being 90.5%, and in a third the same peas at 9 cents, the profits being in this case 114.3%. They then learned that prunes whose wholesale price was 8½ cents a pound, could be bought by the consumer in two of the stores for 10 cents, and one of these also at 15 cents, a case of not letting the left hand know what the right hand was doing. In one of the stores you could buy Santos coffee, costing at wholesale 18½ cents, at 28 or 38 cents, according to your order, whether it was for the lowest or the highest

[1] *Hearings of the Committee on the Judiciary* (1914), pp. 1558-1563.

[2] *Hearings before the Int. & For. Com. Com.*, Feb. 27, 1914, to Jan. 9, 1915, pp. 130-139. Statement of Mr. C. T. Terry.

[3] *Hearings before the Judiciary Committee* (1914), p. 1716.

grade, the range of profit being from 51.4% to 105.4%. They also found that tea in two grades could be extracted from the same can of 25 cent leaves, the prices being 40 and 52 cents a pound, with profits ranging from 61.3% to 106.2%. It was discovered that canned corn, which one of the chains was selling at the rate of $1.08 *and* $1.50 a dozen, could be bought from one of the wholesalers for 80 cents a dozen. . . . It was the same with farina, the quality found in the different stores having a wholesale price of 3¼ cents a pound. The selling prices were different, ranging from 8 to 15 cents, one store selling from the same lot at both 10 cents and 15 cents. In the case of flour, it did not seem to make any difference whether you asked for a low or a high grade, it all came out of the same barrel and at such prices as 11, 12, 13, and 15 cents a pound. . . . The tea which one wholesaler offered to supply at 22 cents a pound, and the three others at approximately 25 cents, could be made to satisfy customers ordering at 36, 40, 50, 60, and 70 cents. . . . Coffee was equally able to take the stage and "play many parts."

A surprising thing was that there was no fixed price for the same article at various stores of the same chain system. Yet the variations under any circumstances could scarcely have been greater. It simply shows what dealers are capable of accomplishing if left to their own devices. The goods so juggled in the above incidents were not standardized or trade-marked goods as a rule. Hence the juggling was done secretly and *upward* invariably. It is contended by the upholders of price maintenance that the juggling of prices on well-known trade-marked goods is accompanied by showy advertising, by wide heraldings, and far-reaching announcements, and is always *downward*.[1] Yet, they say, the motives behind the two processes are the same—to ex-

[1] *Hearings before the Judiciary Committee* (1914), p. 1685. W. H. Ingersoll.

tract more money from the customer. The methods, though different in form, are equally reprehensible, for both are deceptive to the consumer. The injury in the second case is more extensive, however, for not only is the customer deceived indirectly, but the producer is injured, and a chain of forces set in motion which may result in driving the discounted goods from the market.[1]

In the case of the unknown goods only the consumer could suffer from the juggling. As the goods were unidentifiable, the manufacturer could in no case suffer, and the fellow dealers are in no way affected to their injury, as no accurate comparisons can be made between the unidentified goods which he carries and the unidentified goods of others.

Hence it is asserted that price-cutting has evil effects only for the goods which are standardized.[1] This element of standardization is a great blessing to the consumer today. Without it buying would be more or less of a gamble. Imagine the bewilderment of the customer and his helplessness in the hands of shrewd dealers in these times of innumerable types of commodities were it not for the familiar trade-marks that stand out like beacon lights, pointing the way to a known and tested quality, to a reasonable and unvarying value, to unchanging quantity, size, weight and utility.

Furthermore, it is pointed out within recent years such commodity standardization has developed with amazing swiftness. A good of a given type, of a given quantity and of a given value is equipped with a definite, uniform identifying mark — the trade-mark. As a rule, the manufacturer of such a good sees that every unit of it is of exactly the same and unvarying quality, form, weight

[1] *Price Juggling*, address by W. H. Ingersoll before U. S. Chamber of Commerce. Published by the American Fair Trade League.

and size, in every respect. Hence a single testing of the good serves to test its desirability. The consumer knows how to find it again, or how to avoid it. The purchasing process with respect to such goods has become so easy and simple that even a babe may perform it satisfactorily. Maximum ease of purchase, then, and absolute assurance as to quality are in this manner procured.

It will be admitted that any force which lessens these advantages is harmful. A certain type of price-cutting may do this, because, as previously shown, it shortens the life of the article subjected to it, and in many instances drives it entirely from numerous markets. In the one case the consumer has lost completely a commodity which he desired, and in the second case he is put to much trouble and waste of time to find access to the commodity.[1]

As a plea for the integrity of the standardized good the above argument seems ample. The assumption, however, that this integrity is vitally dependent on price maintenance is quite a different matter, and though supported by a few seemingly convincing instances, is by no means justified as a foundation for such sweeping conclusions.[2] The abuses of price-cutting of the nature described are not to be defended, but they can be eradicated by the use of a far less drastic remedy than the one advocated. Why change the nature of the whole distributive system in order to restrain a few perverse retailers? Why use a trip-hammer to crush a flea; or utilize for a surgical operation an axe when a delicate lancet is sufficient? Only the type of price-cutting which injures should be eliminated.

But the other type, the profit-yielding, should not yet be

[1] *Hearings before Committee on the Judiciary*, p. 726, Mrs. Frederick (1914).

[2] See Prof. S. M. Lindsay's testimony before the Federal Trade Commission, Oct. 3, 1917; reported in *Women's Wear*, Oct. 4, 1917, p. 17.

abandoned. The following pages will endeavor to establish that its retention cannot bring injury either to manufacturer or to consumer, and certainly not to those dealers who are efficient. In fact, such price-cutting should be confined to the more efficient. Those who cannot afford it should not practice it, and furthermore should not be allowed to practice it. The inefficient might suffer somewhat in case their patronage should overlap that of a more efficient dealer. Some of the marginal dealers in highly competitive centers would, perhaps, be entirely eradicated. But why not? What principle, either ethical or moral, would uphold the economic weakling as against the best interests of society as a whole?

Let us test the strength of this position by the criteria of quality and service. Will profit-yielding price-cutting endanger the integrity of package goods? Evidently not, for an entire decade of price-cutting, to a large extent legally sanctioned, and hence unrestricted in many cases, has failed to check the popularity of package goods or the interest of the manufacturer in their production. Package goods have reached their highest point of development, not because of price protection, but despite every form of price-cutting. It follows that a rational form of price-cutting is in no danger of eliminating them if the popular taste for them continues. That the popular desire for the package goods is deeply ingrained is indicated by the efforts of such committees as Mayor Mitchel's Food Committee to create a larger demand for goods in bulk. The recent fight in Canada over the elimination of package goods as a war measure, at a time when the temper of the people was prepared as never before to accept economies, is further evidence that the position of the package good is at present impregnable.[1] The same conclusion can safely be drawn with re-

[1] *Printer's Ink*, Nov. 1, 1917, pp. 19-25; Dec. 20, 1917, pp. 71-76.

spect to proprietary and trade-marked goods in general. With the public mind thus receptive, what has the manufacturer with a specialty of merit to fear from the limited price-cutters? Why should he object if an efficient dealer with low operating cost chooses to accept a 20% gross profit rather than 30%, if by so doing he secures a larger turn-over and reasonable net earnings? In the immediate neighborhood other dealers less efficient may be reluctant to handle the commodity thereafter. Their decreased sales will probably be more than offset by the increased sales of the efficient dealer. Outside the circle the less efficient dealers will be unaffected, hence such a thing as a resultant general epidemic of price-cutting would be impossible. These considerations warrant the conclusion that the privilege of price-cutting should be granted only as a reward to the efficient, and in proportion to their efficiency. This principle enforced by legal sanction will take all the sting from price-cutting, afford to the manufacturer every incentive to popularize and widen the distribution of his specialty, but at the same time withhold from him the power arbitrarily to maintain prices regardless of public interest.

To the progressive dealers such an arrangement would be acceptable. The privilege of using at any time the limited cut-price would be a thing well worth striving for. To attain it a dealer would be encouraged to institute all possible economies, especially if he catered to less well-to-do customers. On the other hand, certain dealers might prefer to cling to the normal price, depending on service to attract their customers.

The consumers would profit if they cared to do so. To them would be transferred the benefits, in the form of lower prices, which arose from the economies practiced by the more efficient dealers. It might mean paying cash down,

or carrying home one's purchases under the arm, or foregoing the use of a telephone, but if such inconveniences result in money-saving, the great majority of Americans will cheerfully assume them. Those who desire elaborate service should pay the price for it. Those who do not care for it or to avail themselves of it, should not be charged therefor. The realization and application of these principles are becoming more manifest every day, as is evidenced by the remarkable growth of "economy stores" of various kinds and the innumerable self-serving restaurants.

Price-cutting of the kind here advanced, limited in degree, and made to depend on efficiency, cannot in reason discredit goods in any market or reduce the general demand for them; can in no way deprive the manufacturer of economically justified marketing advantages, offers to the dealer rare opportunity of excelling, and enables the consumer to reap more easily and more abundantly the benefits resulting from efficient retailing.

Additional References

See the issues of *Women's Wear*, Oct. and Nov., 1917, for good reports of the hearings before the Federal Trade Commission, relative to Price Maintenance.

See also, *Hearings before the Interstate and Foreign Commerce Committee* (House) from May 30 to June 1, 1916. Quality and service considerations discussed by Mrs. Heath, pp. 184-195, and by Mrs. Christine Frederick, pp. 148-182.

CHAPTER VI

Price Maintenance and its Relation to Retail Prices

After all has been said about the desirability of price maintenance from the standpoint of the manufacturer; its protection to retailer and jobber; its contribution to better service in salesmaking; its potency affecting quality in the commodity; there yet remains unsolved the main issue—will price maintenance serve to enhance prices, or make impossible of realization any hope for a less expensive distributive system?

Let us devote ourselves first to the question: will price maintenance as a generally accepted policy tend to decrease or increase the prices of identified commodities to the consumer? A brief for those favoring price maintenance would deny that it makes for higher prices on the average. Just the opposite effect would be claimed, the argument being substantially this:

The manufacturer in price-making must take note of competitive conditions.[1] Even though his commodity be a novelty and patented, he cannot escape the probability of the appearance on the market of a good sufficiently similar in all respects to be offered as a substitute. The success of the substitute as a competing good will depend largely on the fairness of the price upon the pioneer commodity. The wise manufacturer will recognize this. Another check to the making of an unduly high price is the well-known principle that usually the volume of sales varies inversely

[1] Gerstenberg, *Principles of Business*, ch. xix.

with the price, and volume is a thing to be desired rather than large profits per unit, for it gives birth to many benefits: such as a decreased cost of production per unit; a firm hold on a wide market; an intangible but highly valued property called "good will"; a decreasing probability of successful competition from another.[1]

The manufacturer having thus arrived at a fair price, it is important that he maintain it, because its maintenance will diminish the burden of risk which the manufacturer must carry. It brings to his service one more constant factor to help offset the world of variables. This constant factor gives him two new advantages, the ability to advertise a price without fear of the falsification of the advertisement by dealers and the ability to apportion a definite profit to the distributors. To be able to advertise *a price* adds to the strength of his appeal to the buying public. Identification of the goods can the more readily be made when one knows the price in addition to the general appearance, trade-mark or brand; and the general public esteem in which the good is held as a result of its quality or form inducements may be appreciably enlarged by an added price inducement. Exceptions to this often occur when the fixed price is one appreciably in excess of the price on competing goods. Other characteristics must then be stressed in the advertising with but slight or no reference to price. Yet the desirability of the fixed price even in this case does not disappear from the manufacturer's viewpoint. The incentive still remains to keep the commodity up to the highest possible degree of prestige and popularity by the general recognition of a uniform price.

The advantage of being able to apportion definitely to the jobbers and retailers their percentage of the gross

[1] A. W. Shaw, *An Approach to Business Problems*, chs. xiv and xv.

profits is of great value to the manufacturer. It means that during the early period of the life of a commodity when it especially needs the support of the distributors, he may secure this support by guaranteeing to them a wide margin of profit in return for their active patronage. As the demand for the commodity grows, in case it does grow, the position of the manufacturer relative to his distributors becomes increasingly better, and when the strength of the demand has reached the point where the goods virtually "sell themselves" the manufacturer may control dealer profits with a considerable degree of success, lessening them or enlarging them as general marketing conditions seem to demand.[1]

The strategic importance of such a commanding situation cannot be easily overestimated. It may enable the manufacturer to effect a compulsory co-ordination of dealers' efforts and advertising so perfect as to insure not only a large but a sustained volume of sales. This condition prevailing, the manufacturer, provided the demand for the good is elastic, and the production of the good in accordance with the law of decreasing costs, is favorably positioned for general price reductions without in any way sacrificing his earnings. He is all the more likely to grant these reductions in the face of real or potential competition, one of which may be said to be always present.

The interests of the dealers would be in harmony with the program of the manufacturer, for in connection with the handling of a standardized, highly-advertised commodity there is virtually no risk except from forced price-cutting. Price-cutting under price maintenance being impossible, the risk of the dealer would therefore be negligible. Such being the case, he can operate safely and profitably on narrow

[1] *Cf.* H. R. Tosdal, "Price Maintenance," *Am. Ec. Rev.*, vol. viii, p. 301.

margins. In other words, he will gladly accept small profits per unit when the number of units sold is large, and when the sales are made with such ease and small expense as occur in the circumstances under discussion.

This represents fairly the case for price maintenance with respect to its possible effects on prices. As *a priori* reasoning it appears plausible, and it is not unsupported by tangible evidence.[1]

But a careful and impartial view reveals a negative case of equal plausibility. After all is said and done, the fact remains that under a price-maintenance system the producer, and the producer alone, sets the price which the consumer shall pay. Though economic conditions do often restrict him to a price which is virtually competitive, they do not always so restrict. In fact, the industrial history of this country proves conclusively that in the matter of price-making artificial devices have frequently triumphed over all normal economic forces.[2] This objection, to be discussed more at length later, does not apply of course to all cases.

However, the next objection does generally apply: that the maintained price is a uniform price regardless of the extent of the market or varying market conditions. The consumers in any given part of the country would be obliged to pay the same price as consumers in any other part. A rigid and unyielding sameness would prevail so far as the consumer is concerned. At this point comes into high relief the main purpose in giving detailed data in previous pages as conclusive proof of the great variance of the cost element in the retailing business.[3] Facing these great variations, the manufacturer in his price-making to the con-

[1] *Cf. supra*, pp. 39 *et seq.*

[2] Stevens, *Unfair Competition*; Ripley, *Trusts, Pools, and Corporations.*

[3] See pp. 55 *et seq.*

sumer, in order to afford a profit to all his distributors, must be governed not only by his own costs, but by the costs of the *least efficient* distributors. He cannot even take the average cost of the distributors, because even they would be less than the costs of the least efficient. To afford, then, a profit to all from the most efficient to the least efficient, while maintaining a uniform consumer price, cannot be accomplished economically under price maintenance, for in practice the manufacturer can handle the problem of distributors' profits in only two ways. He may, in addition to the uniform consumer price, have a uniform wholesale price, in which case the margin between the two must be ample to recompense all types of dealers. Or he may, while maintaining a uniform consumer price, have a graduated price scale for wholesalers. Under the price-maintenance program as advanced so far, there is nothing to prevent preferential discounts. Essentially uneconomic and illogical, however, is a system which permits variegated prices to dealers while requiring uniform prices to consumers. It means that benefits arising from favorable cost conditions never reach the consumer. They are arbitrarily stopped when the goods reach the shelves of the retailer. Or, assuming the existence of unfavorable cost conditions, they may not be reflected directly in the local price but must be distributed indirectly over the entire market, either through the agency of a uniformly higher retail price or by means of a preferential treatment in some form of the unfavorably conditioned dealer.[1]

To be sure, in the absence of price maintenance, the manufacturer has the right to fix the price to the jobbers, or even to the retailers, when he sells direct to the latter. He also has the right, and exercises it freely, to give preferential discounts, and such preferential discounts may be

[1] *Hearings before Int. & For. C. C.*, Jan. 5-11, 1917, pp. 159-169.

passed on to the retailer, and in case of large retailers, always are. But there is nothing to prevent the passing of these benefits or any others still further, even to the consumers themselves.

What proportion of the country's dealers are in a position to sell goods at a price appreciably less than the fixed uniform price to be expected under price maintenance, is of course to a certain extent problematical. But the investigations of the Harvard School of Business Administration and of the Federal Trade Commission lead us to believe that at least 25% of the country's dealers may be so positioned. Hence it does not seem that only a fortunate few consumers would be benefited by economically justified price-cutting. The proportion of consumers benefited would probably be larger than that of dealers, as the most efficient dealers are as a rule in the centers of population and enjoy a business above the average in size. Their economies are real ones. Their price-cutting, if done in proportion to their economies and no more, is economically merited. They deserve fully the resultant benefits. Under a price-maintenance system such economies as certain distributors may achieve cannot be transmitted to the consumer. On the other hand, the lack of economies on the part of the less efficient dealers demands indirectly a premium in the nature of a uniform fixed price just high enough to afford adequate profits to the inefficient distributors. A marked contrast is this, where on the one hand local freedom in price-making allows local economies to be reflected in decreased local prices, and where on the other hand rigid price maintenance not only prevents local price decreases as a result of local economies, but in addition indirectly sanctions the lack of local economies by the maintenance of unduly wide profit margins.[1]

[1] The Federal Trade Commission ascertained that wholesale costs of

Another consideration which should be taken into careful account is the fact that the type of goods within the price-maintenance program is subject to laws in the matter of their price-making considerably different from those which prevail in the pricing of staples or unidentified goods.[1] The latter classes are subjected absolutely to general competitive conditions and, in the absence of monopoly, cannot be marketed successfully at a price above the general level then ruling in the given market. Now put these goods in packages or cartons with distinctive wrappings, or impart to them peculiar form or markings, unique quality, or unusual coloring, affix thereon a brand, trade-mark, patent or copyright notice, and immediately they cease to become staples or "just goods"—they have become specialties. And by that transformation they are lifted above the influence of the normal usual forces in competition. A much higher maximum price-limit becomes possible.[2] Purified middlings are purified middlings the country over, with prices varying only with the general wheat situation. Put these middlings into a package and stamp thereon "Cream

operation varied from 6.3% to 10.71%, the average cost being about 8%. Mail order and grocery jobbers had a still lower cost,—from three and one-half per cent to four per cent. Yet Old Dutch Cleanser fixed prices to jobbers which guaranteed from 11% to 14% profits on the fixed price to retailers,—profits much larger than the average. (See *Printer's Ink*, Sept. 12, 1918, p. 61.)

From the *Hearings before the Interstate and Foreign Commerce Committee on H. R. 13305* (Feb. 27, 1914 to Jan. 9, 1915) the following statistics are taken. They indicate the gross profits allowed to dealers by manufacturers of standard price, trade-marked commodities. Kolynos 50%; California Fig Syrup 50%; Castoria 50%; Listerine 50%; Packers Tar Soap 70%; Eskay's Food 50%; Horlick's Malted Milk 33⅓%. Twenty-seven other commodities are listed which insist on the dealer's taking an average gross profit of about 43%.

[1] *Cf. Annals of Am. Academy of Pol. & Soc. Sci.*, March, 1919, p. 272.

[2] *New York Times*, Sept. 19, 1915; "The Movement to Maintain Prices."

of Wheat," and behold a new product is created, which can be sold at a price largely independent of the price of wheat or of middlings. Tea is tea the world over, and under this cognomen is priced according to the laws of supply and demand. Confine it in packages under the label "Imported Ceylon,"—it becomes a star and dwells apart. Ingredients of a certain proprietary medicine exhibit no magnificent healing properties until, associated with the magic name *Peruna*, they are dragged into the limelight of fame. Hams were merely hams, and lowered their price meekly enough in times of plenty, until they attached to themselves the sustaining brands now so well known. But why multiply instances? They would grow wearisome. Besides, we have given enough to illustrate our point, namely, that in dealing with branded goods we are dealing with a class which to a large degree is immune to the laws of supply and demand, and which in consequence can be priced at a figure largely disproportionate to the costs of production and to the prices of other goods which are similar and of equal value but unbranded.[1] Not the laws of competitive price, but the laws of monopoly price prevail.[2] This does not, of course, mean that the prices fixed will be necessarily extortionate, because even in monopoly price there are certain well-defined price-limits which cannot be transcended with impunity. The principles of substitution and

[1] Address by F. H. Rike at Convention of Nat'l Retail Dry Goods Ass'n. 1916.

Excellent evidence relative to the comparative merits of branded and unbranded commodities is offered by Mr. Straus of Macy's in the *Hearings before the Foreign and Interstate Commerce Committee of the House*, Jan. 5-11, 1917, pp. 125-132. Among the articles discussed are Cream of Wheat, Quaker Oats, Farina, B. V. D. underwear, Vaseline, Cuticura Soap, shaving soaps, Campbell's Soups, etc.

[2] Cyrus B. Miller of the Federal Food Board of New York says, "On the average, advertised package goods cost at least 35% more than the same in bulk." *New York Journal of Commerce*, Jan. 22, 1918.

elasticity of demand forbid such. But it does mean that the composite price-level of branded goods may be easily far in excess of the general price-levels, and in reality this is exactly what does happen.[1] There are many causes which contribute to make possible such a situation.

Probably the most powerful of these causes is advertising.[2] So potent is it that by its liberal use almost any imaginable type of good can be made an object of general demand throughout the country. The article in question need have no virtues to commend it above other brands. If it is of fair quality only, advertising will do the rest. The investigations of Mayor Mitchel's Pure Food Committee have established without doubt that many branded and standardized goods are enjoying wide sales which are in no way superior to similar articles in bulk. This no doubt is the conclusion of many individuals from their own private observations. Yet no intelligent person will condemn the package system or think of discounting the value of the brand. But why should one in his enthusiasm for the package and the brand advocate a system that would raise a protecting umbrella over *all* brands without discrimination, and make possible the marketing of virtually any type of good with comparative ease so long as it is backed up by great advertising capital?[3] The ethics of such a position is

[1] See report of Mayor Mitchell's Food Commission, Jan., 1915. Also *Hearings of I. & F. Com. Com.*, Jan. 5-11, 1917, pp. 136, *et seq.*, 124 *et seq.*, 207, 210 *et seq.*

Mr. E. L. Howe, Sec. of the National Retail Dry Goods Association, says, "The price to the consumer generally upon merchandise which has been branded and nationally advertised is higher than that price at which the same or equally good merchandise, unidentified, unbranded, and not nationally advertised can be purchased by the consumer." *Hearings before the Interstate and Foreign Commerce Committee*, Jan. 5-11, 1917, p. 290.

[2] *Harper's Weekly*, Dec. 4, 1915, "Fixed Prices" by F. C. Pinkham.

[3] French, *Advertising, Social and Economic Results*, ch. iv.

certainly questionable, and even more so is any attempted economic justification. Under conditions now existent, intensive advertising is looked upon as being virtually indispensable to success in marketing branded, standard-priced commodities on a large scale. Perhaps no other single device in the field of distribution of commodities is more efficacious. No intelligent man today questions its great social and economic value. Yet the fullest recognition of this need not blind one to the dangers that lurk in the train of unrestricted advertising. The principle of *laissez-faire* in connection with big business was once regarded as sound. The theory of mercantilism was once so looked upon. As conditions changed the theories arising from them changed. In connection with advertising the conditions are certainly not static. The types of advertising are increasing; the advertising media become more and more numerous; the extent of the appeal is wider and wider; the sum total of the commodities to be advertised becomes greater and greater with no limits to its growth in view; the competitive warfare between goods of similar lines becomes ever more intense with each addition to their numbers.[1] The expenditures for advertising are enormous, and rapidly increasing, with no probable limits to their expansion in view. With this growth in the intensiveness and extensiveness of advertising there is an increase in its power to misrepresent and deceive. That this power is used by certain advertisers we know both from personal observation and from official investigations.[2] Happily such deceptive practice is not general, but instances of it are sufficiently numerous to indicate the necessity of careful procedure in the creation of new stimuli to advertising unless they be accompanied by

[1] Copeland, *Business Statistics*, ch. iii.

[2] *Printer's Ink*, Sept. 12, 1918. Action of Federal Trade Commission against certain advertisers.

the development of higher positive standards and effective negative restrictions.[1] Most probably no greater stimulus to advertising could be devised than the institution of price maintenance. As noted above, the power to fix the price carries with it the power and encouragement to advertise a price as a special inducement supplementing quality and quantity inducements. According to price-maintenance supporters this must put the manufacturer in that favorable position where large volume and lower unit cost tempt to lower prices. But is not human nature so built that such a temptation would be offset by a desire to attain yet greater profits and a stronger hold on the market? The result would be still more advertising. Those surplus profits which we love to think of as making possible price decreases would very probably be diverted into advertising. The same weapon would, of course, be resorted to by competitors. Other things being approximately equal, to the most profuse and skilful advertisers the victory would ultimately go. The competitor without advertising capital would be at a very great disadvantage. Howsoever desirable his product might be, however good the quality, his chances for a wide market would be small, especially so if the commodities against which he was competing were already well established. Price maintenance in connection with advertising is a weapon of cumulative effectiveness, the effectiveness increasing in a progressive ratio as the demand for the advertised product increases.[2] To make this point clear, let us assume that the maker of a certain brand of breakfast food has, by virtue of heavy advertising and a fair product, secured for his good a wide and active market. The mag-

[1] Testimony regarding price maintenance in its relation to advertising may be found in the *Hearings before the Interstate and Foreign Commerce Committee of the House*, Jan. 5-11, 1917, pp. 90-97, 170-180, 382.

[2] *Hearings before Committee on Judiciary*, 1914, p. 893.

nitude of his volume puts him in a position to offer special inducements to his distributors either directly by offering them wide margins of profit to push his good, or indirectly by providing for them still more advertising in order to accelerate their turn-over. In their turn, being assured of a dependable market, the dealers are willing and anxious to "push" the product. Dealers naturally are in business for profits, that is, most of them are. It is no surprise that their chief criterion in selecting goods for resale is profitableness. It is a matter of common comment that most dealers push the goods which afford the highest profit. These things being true, it is easy to surmise the difficulties which the young rival will have to meet and overcome before he can compete successfully with our well-established manufacturer of cereals.[1] In this hypothetical case which we have chosen the difference between the respective advantages with the two manufacturers possess in the market is not the sort which is natural and inevitable from purely economic or social reasons. It is, on the contrary, a difference artificially emphasized and enlarged by the purely arbitrary power of the legally maintained price. After all, the weapon of price maintenance is of but small value to the weak or to the young hopeful. (Few care to cut the prices of the virtually unknown, anyway.) It has virtue chiefly for the powerful, making them more powerful. Its efficacy increases with a rapidly accelerated progressive ratio once its possessor becomes strong. Hence a manufacturer once well established in the field with a wide market developed, as we have stated before, can command the unswerving loyalty of his dealers. With the power of price maintenance to help him keep in line all dealers who have a tendency toward perverseness, he becomes all the more

[1] "The Retailers' Point of View," speech by Donald Dey before U. S. Chamber of Commerce, Feb., 1914.

strongly entrenched.[1] No competitor could successfully cope with him, except by a prodigious outlay of capital and effort. Under such circumstances all motive for price reduction would be considerably modified, so far as the manufacturer is concerned.[2]

From still another viewpoint there is apparent an additional force leading to the same danger. Wherever the production of one general class of commodities is in the hands of a few equally powerful competitors, the competitive situation would be a very undesirable one. The resultant advertising war would call for lavish expenditures. It would not be possible for any one of the competitors to decrease prices locally, for under price maintenance local price decreases would be forbidden. Any price changes would have to be uniform and general. A lowering of price sufficient to affect the situation so far as competition is concerned would therefore entail severe losses—too heavy to be borne for any great length of time. At present, losses to meet competition in one part of the field may be offset by profits in another. Moreover, under price maintenance, the general price decrease could be restored only with great difficulty in the absence of an increase in the general price level. The public will with perfect equanimity accept increases in the price of unbranded goods or staples, because here they know that the laws of supply and demand are at work and cannot be gainsaid. No such attitude could be expected toward branded goods. Even if each of the competitors should be persuaded to effect a general lowering of prices by the stress of competition, the situation would not be relieved. The history of competition teems with examples of powerful interests engaged in such conflicts, and practically all of them demonstrate that such conflicts

[1] *Annual Report of the Federal Trade Commission*, 1918, p. 130.

[2] *Women's Wear*, Feb. 18, 1916. Article by B. R. Kobey.

end in some sort of agreement or combination. The incentive to such agreement would be stimulated by price maintenance, not only because of the greater costs and possible disasters of competition under such a régime, but also because of the greater temptations which such a régime would afford. Collusion or agreement of some sort, carrying with it the power of the fixed price through every stage in distribution, would in its attractiveness be well-nigh irresistible. In fact, it would be the only haven of safety in the situation we have described. The machinery of such agreements under price maintenance would be reduced to a minimum, in fact would be so simple as to insure their success and durability. Illegal they would be certainly, but no law is of sufficient virtue to reach every contingency. For instance, it cannot reach the present "community of interests" situations that exist in the oil and tobacco industries, not to mention numerous others. The point is further illustrated by reference to an incident in the drug industry, as related by Wm. J. Shroder, a prominent Cincinnati attorney. The facts were brought out in the federal courts (U. S. *vs.* National Ass'n of Ret. Druggists).

I was one of the attorneys in this case against the National Ass'n of Retail Druggists. The investigation developed that the resale-price-maintenance movement began with the efforts of the Western Ass'n of Wholesale druggists as far back as 1876.

In 1881 these druggists in order to stop competition between themselves, urged upon the members of the Proprietary Ass'n of America, who were manufacturers selling trade-marked goods in the drug trade, the adoption of a rebate plan by the terms of which a wholesaler was sold at list—that is, the same price at which he was supposed to sell to the retail dealer—and received his profit upon signing a contract to the effect that he sold to the retail dealer at a certain price which was deter-

mined by the Association. This simple plan of resale price maintenance, with modifications, remained in effect until 1898, when the National Ass'n of Retail Druggists came into being. Instantly, in the language of one of the witnesses before this committee, the "let-us-get-ours" talk commenced. The result was a conference between committees of the Proprietary Ass'n of America, and the National Wholesale Druggist Ass'n, and the National Ass'n of Retail Druggists, which developed what was known to the trade as the "tri-partite" plan. This was a three sided agreement in which the manufacturer agreed to sell his good to the wholesaler, and to confine his sales to such wholesalers only as appeared upon the recognized jobbers' list, which was prepared by a committee of the National Wholesale Druggists Ass'n, and contained only the names of those who had agreed to maintain a certain price to the retail trade. The wholesaler also agreed that in his sales to the retail trade he would not sell any retail dealer whose name appeared upon the black list prepared at first directly by the National Ass'n of Retail Druggists, and ultimately by a publisher employed by them. This black list contained the names of the dealers, and the suppliers of the dealers, who sold goods at competitive prices.

This plan to a certain extent depended upon the good faith of the parties to it. When a dealer acted in bad faith, and was not caught by the detectives and spies of the associations, there was no way of determining whom he was supplying, or whence the prohibited dealer's supplies came.

In order to meet these conditions, the associations urged upon the proprietors the adoption of a resale price maintaining contract, with serial numbers identifying the articles, requiring the wholesale dealer to report to the manufacturer by serial number to what retail dealer he had sold the particular item of his sale.

The Dr. Miles Medical Co. adopted a direct-contract serial-numbering arrangement for marketing its product, at the direct request of the Retail Ass'n. Because the wholesale ass'n had not been consulted the Dr. Miles Medical Co. was compelled

to withdraw this contract from the market, and after consultation with, and the approval of a committee from the National Ass'n of Retail Druggists and the National Wholesale Druggists' Ass'n adopted a contract. This is, in substance and effect, the same which it is urged to be legalized; . . . a resale price maintenance contract for the purpose of choking off competition from the hands of the producer to the hands of the consumer. . . .

At this point, the United States intervened. The Court enjoined and ordered the cancellation of every contract, every black list, very white list, and in this manner broke up an illegal combination which the trade associations had struggled to perfect, and which they had succeeded in perfecting.

The above "tri-partite plan" was encumbered by much heavy machinery. It included within its grasp not only manufacturers, but wholesalers and retailers. The parties to the agreement were numbered by the thousands, and from the beginning it was tainted with illegality. Yet for a number of years it worked, and in the year prior to its injunction by the Government the Association boasted that it had saved for its members 40,000,000 dollars. Under a price-maintenance régime, an agreement similar in motive to the above but far more effective in its workings could be created merely through a mutual understanding of manufacturers. The dealers would not be parties to it at all—in fact, they would not even need to know of such an agreement. Why should they? They would be compelled to sell at the fixed price at all events. Hence, it is easy to see that by price maintenance conditions would be made ideal for agreements virtually in restraint of trade [1]—in fact, so ideal

[1] The interesting question, would price maintenance be a stimulus to combination or monopolistic methods, meets a partial answer in the evidence that the principal shirt and collar manufacturers of the country acted as a unit in the matter of price raising during the war, the ratios of price increases and their dates of going into effect being the same

that their presence would be almost a certainty despite their illegality.[1]

A mere "community of interests" arrangement would be sufficient. A device similar to the Gary dinners might well be adequate. In any event no parties to the agreement would be necessary *outside the manufacturers themselves.* The less the number, the less the risks, and correspondingly greater the opportunities for excessive profits. This only

as regards all the well known brands. See *Hearings before Interstate and Foreign Commerce Committee,* Jan. 5-11, 1917. Testimony of P. S. Straus.

[1] Since writing the above, more illustrative facts have come to my attention which perhaps should be mentioned.

Many stores, as a result of war conditions which impose the necessity of utilizing all possible economies, have greatly decreased the traditional services offered to patrons. Hence the growing use of the "Cash and Carry" practice, the customers in such case being urged to pay cash, and carry home their purchases for themselves. Resultant savings are metamorphosed into uniformly lower prices. Should certain customers insist on delivery they are charged extra for the accommodation. Similarly an extra charge is made when credit is insisted upon. In both cases the extra charges are approximately equal to the actual cost of service. Chas. M. Decker and Bros. who do a large chain-store grocery business in Northern New Jersey use this system. The results are highly beneficial to all concerned. The number of delivery vehicles was reduced from 68 to 29. A 90% credit and a 10% cash business was transformed into a 60% credit and 40% cash business. Fewer salesmen were necessary and a smaller clerical force. Prices were largely reduced for those customers desiring no extra services. In addition to these economies, self service is becoming more and more popular. The Piggly Wiggly stores, a chain system using self service, have reduced their operating cost to 5%. The Larkin chain also practices it, as do many of the five and ten cent stores. By its use L. S. Ayres & Co. of Indianapolis has reduced its traditional selling costs by 8% of the total selling price, which saving goes to the customers. Bloomingdale Bros. use it in their basement. A. F. Sterne & Co. of Wilkesbarre uses self service exclusively. Forty employees now do the work formerly done by 150, although the rapidity of turnover has greatly increased. These thoroughly legitimate and highly desirable economies with resultant lower prices would be virtually impossible under a rigid price-maintenance schedule.

suggests the overwhelming possibilities of evil with which such a scheme is charged.

Let us now regard the question of costs and prices from the point of view of the dealers. Throughout the country are thousands of dealers who, by means of legitimate economies obtained by the exercise of superior business skill, superior organization, superior location, etc., are able to sell goods, both branded and unbranded, without discrimination at prices lower than the usual. They do not exploit these goods. They sell them at a fair profit. Any system preventing such business methods would arbitrarily increase the living expenses of customers who are fortunate enough to live near these stores.

John D. Park & Sons Co. are wholesale druggists in Cincinnati. For forty years they have conducted their business upon the basis of coöperation between the retail dealer and wholesale dealer. Their proposition has been this: It costs the wholesaler from 6 to 8% to keep traveling salesmen on the road. If the retailer will mail his orders, this expense can be saved. If the retailer will accomplish this saving, it belongs to him and can be used by him for the benefit of the consumer. The John D. Park & Sons Co. have continuously sold all merchandise,—advertised and unadvertised proprietary, trademarked, and anonymous—, at 6% less than list prices. Price maintenance would prevent this method of doing business.

The Kroger Grocery Co. is a chain-store unit of 200 groceries. Thirty years ago B. H. Kroger began business with a capital of $372. His policy with his first store was the same as is his policy with 200. The cost of extending credit, of calling for orders, and of frequent deliveries increase the expenses of merchandising almost 100%. Let those consumers who do not demand this service receive the benefit of the saving. His stores are cash stores—every customer receives the benefit of this saving regardless of neighborhood. Those neighborhoods demanding delivery service pay more

than those carrying their purchases with them. The Kroger stores sell all merchandise, every day of the year, advertised and unadvertised, proprietary, trade-marked, and anonymous, at less than regular prices. Resale price maintenance would stop this.

The Dow Stores are a chain of 10 drug stores in Cincinnati. Miss Dow, their former proprietor, began with one store, 25 or more years ago, with a capital of $500.00. She believed in giving the consumer the advantage of her quantity purchases. Her competitive prices prevail every day in the year and on all merchandise in her establishments. Resale price maintenance would stop this.

The Economy Drug Co. and the Bruns Bros. Grocery Co. are companies whose stock is owned by the independent retailers in Cincinnati and its surrounding territory. Their cost of doing business is 5%. They buy at wholesale in quantities and sell to their stock-holders at 5% above cost. The retail dealers save approximately 10% on their purchases, part of which is given to the consumers. The retail stores sell at less than list prices. Resale price maintenance would stop this.[1]

These illustrations, together with numerous others we might mention, lead to the conclusion that the type of price maintenance now being advocated and urged upon Congress through the Stevens bill is prohibitive of many possible savings to the consumer, realized directly from the retailers.

There are those who insist that justification for price maintenance is found in the experience of certain European states — Germany, France, and England.[2] So very different, however, are general economic conditions in these countries, as well as the attendant administrative and

[1] *From Hearings on Trust Legislation, Committee on the Jud.*, 1914. Testimony of William J. Shroder, pp. 1404-5.

[2] See *Report of Special Committee on Price Maintenance* of the U. S. Chamber of Commerce, p. 73.

judicial machinery, from the analogous situation in the United States that their citation is of practically no value. Furthermore, the economic ideas of both England and Germany are (or were prior to The War) essentially different from ours. The *laissez-faire* doctrine has largely dominated in England, as is evidenced by its free-trade policy. It is quite in keeping with such principles that trade combinations, with their control of markets and prices, should to a certain extent be tolerated, in the belief that every evil will find its own corrective in the absence of governmental restraining influence. American public policy, because of bitter experience with trusts and monopolies, is radically opposed to the traditional English view. Yet it must not be inferred from this that in England price maintenance has free sway. It is by no means accepted there to the extent which is being advocated in this country. It must be also borne in mind that England does not produce monopolies or gigantic manufacturing establishments to so great an extent as does this country. This fact, together with her free-trade policy, which subjects her manufacturers to the full pressure of foreign competition, provides apparently for the welfare of the consumer.[1]

In France the criterion upon which legal action against trade combinations is based is *price enhancement*. Trade methods there are tolerated which in this country would be condemned, and the evils therefrom do not appear to be excessive because the government keeps its eye on *prices*.[2]

[1] An additional safeguard against the excessive and maintained price in England is to be found in the well developed Co-operative Stores system of that country. It contains 1350 stores with a combined capital stock of $235,766,000. The membership list is made up of three and one-half million householders. Sales amounted to $336,000,000 in 1917. As is well known these stores turn back to their customers that part of the selling price which is over and above actual costs. Wherefore in this system price maintenance can have no meaning or effect whatever.

[2] Ripley, *Trusts, Pools, and Corporations*, ch. xx.

In the United States there is no criterion. In the Supreme Court decision relative to the U. S. Steel Corporation, the Court held that mere size should not be considered a condemnatory feature of big business. In the International Harvester case, the Court held that mere size was a condemning feature. A "rule of reason" has been adopted. In guiding the Court, its light is as a wandering fire.

In Germany price maintenance, as would be expected, is universally accepted and is perfectly legitimate.[1] But the German economic system is as different from ours as day is from night—not only in its methods and structure, but in its underlying philosophy. Virtually every form of trade and manufacturing is embraced within the Cartel system. With many of them the government itself is in active partnership. Elaborate administrative machinery is utilized in supervising and regulating the conduct of the Cartels, and the power and activity of the government are far greater, relative to all forms of industry, than would be feasible or tolerable in the United States. As has been said,

The economic policy of Germany is paternalistic in the extreme. It encourages the formation of combinations which the American economic policy and statutes expressly forbid. The people are accustomed to governmental regulation and interference and naturally submit to regulations and control of trade organizations which have the approval of the authorities. Price restriction and price control in Germany are but incidents of the Kartel system which is opposed to the public policy of the United States.[2]

[1] *Rep't of U. S. Chamber of Commerce Committee on Price Maintenance.*

[2] *Rep't of U. S. Chamber of Commerce on Price Maintenance.* Tosdal, H. R., "Price Maintenance in the Book Trade," *Quarterly Journal Economics*, vol. xxx.

Assuming that price maintenance should be legalized in the United States, that through its application and logical consequences certain gigantic manufacturing enterprises should develop into monopolies and fix prices at their pleasure, what would be the remedy of the public? At present we have no machinery, either administrative or judicial, which could legally cope with the situation if it were shown that no *combination* or *conspiracy* was involved. Recognizing the inevitableness of this, Senator Borah introduced a bill providing, in conjunction with price maintenance, machinery for governmental control of such prices as would be affected. This bill does not seem to meet with the approbation of the price-maintenance supporters. They are unwilling to consent to any potential price limitations. In short, the manufacturers, for whatsoever price they ask, wish legal protection but not legal supervision. The dangers of the former without the latter at least have been suggested. Yet the combination of the two seems just at this time equally dangerous. Governmental price regulation as a policy applicable to all commodities, in order to be successful, demands economic conditions far less dynamic and complicated than ours, and administrative organizations far more specialized and efficient than ours are at present or could hope to be for many years under our adolescent democratic régime. However encouraging our governmental ventures into the fields of price regulation have been during the course of the Great War, they fail utterly as yet to afford a safe basis for generalizations contrary to past experience. Since April 6, 1917, economic, political, and psychological conditions have been extremely exceptional. Over all considerations of personal interests or mercenary gains was thrown the cloak of passionate patriotism. Willingness to modify in their economic relations all the accustomed modes of acting and thinking and to accept in com-

mon subserviency modes of conduct prescribed by the government soon became, after the outbreak of the war, a virtually universal phenomenon and made comparatively easy for the government successful application of price regulation in a few of the country's fundamental industries. The endeavor was further facilitated by the simplicity of the motive involved, which was certainly not a desire to establish prices economically correct, but merely to approximate an economically correct price for the purpose of avoiding undue profiteering on the one hand, while on the other assuring adequacy of production by guaranties of abundant compensation for the producer.[1] A motive such as this in peace times would get us nowhere. It would be totally ineffective if obliged to function within the narrow margins which are typical of business operations during normal conditions.

Yet foolish indeed is the man who refuses to see in the events of the past two years any indications whatever of the coming increase in the powers and efficiency of the administrative organs of our government. Behind the dark clouds of war, all but unnoticed, are being carried on comprehensive experimentations relative to problems of price and business ethics which, if carried on a few years ago, would have excited the highest degree of public interest. In the clear air of returning peace the results of these experiments will loom before us with seemingly appalling suddenness. What their form and magnitude will be is uncertain, but assuming that they will go so far as to constitute a vindication of governmental fitness for these functions, it is inconceivable that within the present generation official machinery could be created sufficiently extensive to handle effectively other than those industries which are

[1] *Printer's Ink*, Oct. 10, 1918, pp. 97-106, "Gov't Control of Prices in the Shoe Trade," illustrative.

vested with the greatest public interest, few in number and but an infinitesimal part of the country's activities. A conclusion which predicates any greater degree of control than this is certainly not warranted by the achievements or tendencies of the present, howsoever remarkable they may be. Therefore advocacy of any given policy, such as price maintenance, in anticipation of the adoption of general governmental fixation or supervision of prices, must be unsafe and illogical.

There is one tendency of the times in particular which seems free of all countervailing influences of any importance, and that is a very marked tendency toward a more complete eradication of all corporate powers and privileges not absolutely essential to the successful conduct of domestic business. In marked support of this proposition stand out the recent activities of the Federal Trade Commission, the Federal Courts, the Federal Congress; and no different attitude is being exhibited by the various state governments.

A very distinctive departure from this tendency would be the granting of the price-maintenance power to the manufacturers of the country. That such a power should be given prior to the establishment of adequate machinery for the supervision and control of prices is unthinkable. With a decisiveness that knows no doubt, American public opinion and American law have accepted as their criterion of justice the welfare of society as a whole. If from them any class receives any distinctions of importance they are negative distinctions and not positive; they are in the form of restrictions and not of special privileges. To this criterion we are becoming more closely bound as our democracy develops. In our discussion of price maintenance, the welfare of society is the welfare of the consumer. If price maintenance is a menace in the slightest degree to the welfare of the great mass of consumers, it must be repudiated.

In the absence of certain safeguards it is such a menace—as indicated in previous pages—in that it is not only a bar to the realization of certain legitimate economies, but it is also a positive force in the encouragement and creation of conspiracy and monopoly with the attendant evils.

One of the gravest objections, however, to be brought against the price-maintenance system is that it would tend to ossify or crystallize the distributive system as it now is, and make practically impossible any changes that might lessen the cost of distribution. Students of the problem of distributive costs have never been able to become reconciled to the enormous " spread " between the cost of manufacture and the final price to the consumer.[1] This wide discrepancy between cost price and selling price is a matter of grave concern to the people as a whole, and any innovation, howsoever radical, aimed at its reduction should be allowed a fair trial. The old orthodox method of distribution — from manufacturer to wholesaler, from wholesaler to retailer—has probably reached its most efficient stage. If improvements are to be looked for, they apparently must come from another source. Perhaps the chains, the mail-order houses, the department stores will contribute somewhat to the solution of the problem. It may be found that the functions of the jobber can be more economically performed by the manufacturer or retailer. Valuable lessons may be learned from the co-operative associations and the buying exchanges.[2] Selling through the mail may even-

[1] Taussig, " Price Maintenance," *American Ec. Rev.*, March, 1916.

[2] As a concrete illustration of the possibilities of price reduction lying in co-operative associations, I cite the Philadelphia experiment. There the Community Stores, over 2000 in number, have appreciably lowered prices. Representative prices for the month of May, 1918, were as follows: Babbitt's Soap sold for five cents instead of the usual seven; Lux sold for ten cents instead of the usual twelve; Campbell's Soups sold at the rate of three for twenty-five cents instead of the usual twelve

tually displace the traveling salesman, and the "from the factory to the consumer" movement may not be without its possibilities for saving. Whether or not these suggestions appear plausible to the reader, the fact does remain that we are in a period of active experimentation in the distributive field. It is equally true that we do need more economical methods of distribution. Hence it follows that no premature barrier should be constructed which would block the trial and possible adoption of new devices and methods.[1]

Price maintenance would be such a barrier.[2] It is formed primarily to fit the conventional scheme of selling. It groups together roughly every type of retailer and imposes upon them the same conditions. It makes allowance for the profits of the wholesaler, and provides that wholesalers and retailers shall be kept clearly distinct. It draws between them a sharp dividing line, and prohibits the retailer from assuming the functions of a wholesaler. It is hostile to all such business forms as chain stores, department stores, mail-order houses, co-operative associations, and buying exchanges, by forbidding to them the exercise of economies in buying and transmission of economies in selling, things which to them are the very breath of life. Now these types of retailers have often been accused of unfair tactics in competition. But no one, not even their bitterest opponents, has as yet been able to adduce evidence proving that their existence entails greater costs in distribution. As a matter of fact, all available evidence seems to prove the opposite. That they are a menace to the smaller stores and endanger,

cents straight. What is more striking, the manufacturers in this case seemed not to disapprove of the cuts.

[1] *Women's Wear*, Feb. 18, 1916; Benj. R. Kobey on "Price Maintenance."

[2] *Cf.* Prof. Gephart, address before American Economic Ass'n, Dec., 1915.

perhaps, the venerable offices of the wholesalers and the independence of the manufacturers, may easily be a thing worthy of praise rather than condemnation.

General References

(Price Maintenance in its relations to the Cost of Living):

Hearings before the Interstate and Foreign Commerce Committee (House), Feb. 27, 1914 to Jan. 9, 1915; May 30 to June 1, 1916; and Jan. 5 to 11, 1917.

Hearings before the Committee on the Judiciary of the House, 1914.

Hearings before the Federal Trade Commission, Oct. and Nov., 1917. Reported in *Women's Wear* for those months.

F. W. Taussig, "Price Maintenance," *American Economic Review*, March, 1916.

H. R. Tosdal, "Price Maintenance," *American Ec. Rev.*, vol. viii.

See also Chapters on Price Maintenance in Cherington, *Advertising as a Business Force*; Butler, *Marketing Methods*; Nystrom, *Economics of Retailing.*

CHAPTER VII

THE ETHICAL ASPECTS OF PRICE MAINTENANCE

THE advocates of price maintenance allege as one of their chief arguments that the manufacturer of a branded good has a moral right to fix the reselling price of that good. The basis of this right is that intangible thing called "good will," which inheres in the good by virtue of its established reputation, quality, price, etc. It is assumed that any given trade-marked commodity owes its existence to the enterprise and business ability of the producer.[1] Upon it he expends his fortune, his time, his energy, and his business reputation. If the good does not meet with public approval, his is the blame, his alone the loss. His initiative and his ability direct the distribution of the good. He plans the advertising, he persuades the dealers. He guarantees sales and continued quality. In the beginning his only reward is hope. But under his vigilant and fostering care the market is gradually conquered. Demand increases day by day. The consumers, pleased with the commodity, begin to learn the manufacturer's name and trade-mark. The trade-mark comes to be associated with the idea of that particular commodity and connotes in the mind of the individual the quality, quantity, weight and form values of the commodity in question. He recognizes it at sight and calls for it without exertion of memory. And in proportion to the number of consumers thus

[1] Prof. C. C. Arbuthnot in *Printer's Ink*, July 24, 1913.

affected, the value of that trade-mark grows. It stands as an unvarying identification mark by which they may always recognize the article in question, and select it, rather than accept some competing commodity. This peculiar trade-mark value is to the commodity and the manufacturer what wide business relations and reputation for honesty are to a firm of retailers or contractors. And just as the latter form of good will is valued and capitalized in the business world, so is the well-known and widely favored trade-mark to be valued and capitalized. Now, price-cutting is represented to be the exploitation of this "good will," and hence an ethical violation of the moral rights of the manufacturer or producer.[1] Perhaps the case has been nowhere more clearly stated than in the editorial columns of *Publishers. Weekly* (May 1, 1915).

Sellers of standardized, patented, copyrighted, or trade-marked goods are, it has been pointed out, dealing in two quite distinct things, viz: the actual physical articles they sell, and the assurance of the worth of those articles. If a man buys a Ford Automobile he buys a certain piece of machinery designed for a specific purpose; he also acquires the assurance that that piece of machinery will perform satisfactorily the service he expects it to perform. If a man buys a package of Kellogg's Corn Flakes, he secures a quantity of prepared, cooked kernels of corn; he has also the satisfaction of feeling that he has a nutritious, safe, and palatable food. If a man buys a copy of Churchill's Inside of the Cup, he has in his possession, not merely one pound of ink-spattered paper sewn between two covers. He knows that he has a piece of fiction which several hundred thousand people have acclaimed stimulating and suggestive. Now it is obvious that we have to deal with two diverse sorts of values, one concrete, one more or

[1] "Ethical Reason for Standardized Price," F. W. Nash in *Journal of Commerce*, May 8, 1916.

less intangible, but not less real. It is also obvious with the latter sort of values the individual retailer has little or nothing to do. He buys merchandise of the manufacturer and pays the manufacturer for it. For the market reputation of the manufacturer's goods, a reputation based perhaps on years of effort, and hundreds of thousands of dollars spent in advertising, the dealer, in any one individual case, pays comparatively nothing. The good will or trade reputation of an article is the creation primarily of the maker or manufacturer (of the author or the publisher). The latter may and does allow the retailer to trade upon that reputation. He may and does share it voluntarily with the purchasers of his goods. But that does not, or should not, give them any right in or to it. Good will is obtained by the expenditure in wise union, of brains, energy, and money. Intangible though it may be, it has nevertheless a real property value. It can be given away, sold, or stolen just as any other property can be. It may be objected, however, that though these two sorts of value inhere in every standardized, patented, trade-marked, or copyrighted article, it is difficult, or indeed, quite impossible, to separate them. But is it?

Unless we are mistaken, a well known trade-marked watch company once made an offer to a certain notorious price-cutting department store, in substantially these words: "You state that you are cutting prices, only to afford your customers the lowest possible prices on a standard piece of merchandise. You add that you are having difficulty in securing supplies of the article in question. We state that you are cutting prices for advertising purposes; utilizing the good will we have created—our property—to effect profitable sales in other lines of merchandise you carry. To prove our point we will make you this offer: we will sell you all our watches you desire at our regular prices without restriction, but on the one condition that you do not with them trade on our reputation, that is, that you do not sell them as Blank watches, but under some private name that you can select. We guarantee that the watches will be the same watches in every respect but name. Simply you will not be able to exploit our watch's reputation

for what we claim to be private advertising purposes. You will, according to your own statement, serve your own public just as well, but at no trouble to yourselves." The department store is said to have ignored the offer.

Is it impossible to separate the material article and the abstract good-will value added to that article by author and publisher? Let us see how it would work out in the book trade. Suppose some isolated store started out for the transient advertising gained to cut prices on "The Inside of the Cup" aforementioned. Would it not be possible for the publisher of that novel to go to that price cutter and say, "You claim your only desire is to give your customers full value received for their money. I claim that in attempting to cut prices on The Inside of the Cup, you are destroying the author's good will, tending to render the sale of his books at retail difficult, or impossible, in short, stealing his property. If you are sincere in your protestation, you will accept this offer: I will sell you all the copies you want of the Inside of the Cup, by Winston Churchill, identical word for word, book for book, in every way, except your special edition will be *The Sins of Ahinoam*, by James Smith, and you are not to suggest in any way, directly or indirectly, that your book has any relation whatsoever to the Inside of the Cup. Advertise it all you wish; create for it all the good will you can, but don't tear down for your personal gain the good will that I have built up for the original book. If it be true that all you are selling is merchandise, your patrons will be getting just as much, no matter what you label it. If it is, on the other hand, true that when you sell an advertised book you are selling a piece of merchandise, which is your property to do with as you please, and, in addition, a reputation for that book which is not your property at all but mine, then your patrons would not buy your labeled book as they buy mine."

The above conversation possibly makes clear a point, sometimes obscured. When a retailer buys outright a standardized, patented, copyrighted, and trade-marked article he does not, as the legal phrase runs, buy "all right, title, and interest of

every sort therein." The good will in the article, by common justice, as well as legal precedent, remains with its creator.

It is interesting to contrast this "moral right" of the manufacturer to maintain prices by virtue of the good will in his brand with the "moral right" which the price-cutting retailers claim. In this latter instance the right is based on *title*. The retailer says in substance:

I have bought these commodities. For them I paid the price asked by the manufacturer. I do not sell them as an *agent*; I sell them as an *owner*. The title to them, according to all law and precedent, is completely vested in me. They are mine to do with as I please. Why should the manufacturer who has received his price, who has made *his* stipulated profit be privileged to say what *my* profits shall be? Years of experience have taught me that price cutting is conducive to better business, that often it is not only desirable, but absolutely necessary. This being true then, why should I be forced to follow a policy pleasing to a man who not only knows nothing of my business needs and policies, but also has no vestige of title or equity in the goods I am selling? In short, who is this manufacturer, that he should dictate to me how to run my business?

Quite obviously these alleged "rights" are in hopeless conflict. In both there is an element of justice. Yet neither of them can be wholly approved, because there must enter into consideration the "rights" of still another party, and this third party is the great public. Viewed from the standpoint of the public interest, how absurd seem the arguments of both manufacturer and retailer as to moral rights. Their logic fades into a mere dead form. For what rights are there, except those that are socially derived, and these are not given for an eternity, but only for the period of the then existent set of circumstances. Wherefore pools, monopolies and price discriminations in their time have

been both legal and honorable. Modern public policy has put upon them the stamp of its disapproval, and now they are both illegal and dishonorable. In like manner there was a time when the unrestricted power of price maintenance could have been lodged in the hands of the manufacturer with perfect impunity. That was the day before big business, national advertising and national marketing. Then no manufacturer could have used such power harmfully; his market was limited, his scope of influence was narrow, the brand was but little used, was but locally advertised, and included almost none of the necessaries of life. Practically no commodities were of the identifiable type, except copyrighted and patented articles; while the staples were not only unidentifiable, but largely local in their origin and use. No one producer or set of producers were looked upon as being very potent factors with respect to the public welfare. To indicate how different conditions are today, I have but to mention the names of such producers as the American Sugar Refining Co., Armour & Co., Swift & Co., American Tobacco Co., U. S. Steel Corporation, Standard Oil Co., the American Corn Products Co.

No thinking man for an instant would concede that these companies should be allowed to perform any act justified solely on the grounds of their so-called "moral rights" without weighing first the possible effects of such action on the public welfare.

Why this changed attitude? Because these companies have become *virtual* public utilities.[1] Their distinction from real public utilities is one arising not so much from difference in kind, as in degree. They have arrogated to themselves so important a part in administering to the wants of the people that they can no longer perform it lightly or

[1] Bruce Wyman, *Control of the Market.*

wilfully, but only in accordance with the demands of the people. They have no rights that extend beyond the limits of this principle. Social recognition of this is leading rapidly to general legal recognition. From transportation lines, bridges and canals the principle has extended itself to include gas, electric, water, telephone, and express companies in increasing varieties and numbers — companies which a few years ago boasted of their rights to do business as they liked, but which are now closely supervised as to methods, charges and profits in many of the states and cities. Their classification as public-service utilities and consequent treatment as such is purely a matter of public welfare. Their relation to some given public need or want has been the sole and sufficient criterion. Obviously such a criterion does not afford the opportunity of drawing a sharp and logical distinction between public utilities, so-called, and the virtual public utilities to which I alluded. Let us assume now that to these latter the power of unrestricted price maintenance was accorded. It does not require a sage to perceive that the exercise of such a power might easily be contrary to the general good. Governmental control of some kind would then be inevitable as to prices, profits or methods.

Our conclusion, hence, is that, howsoever great be the industry of the producer, the brains, the skill, the energy or the toil he has exercised; howsoever great the responsibilities he has assumed, the risks he has shouldered; howsoever precious to the people be the product which his genius, his capital, his energy have united to create and to establish in the markets of the world; howsoever enormous the fortunes he has spent in consummating his ambitions in any way; despite all these things there attaches to him no moral right to fix all prices over the heads of jobbers, wholesalers, retailers and consumers, with no consideration of the other

interests involved. Such a right, if universally bestowed, would make of the distributive system an economic feudalism, with the consumer as the unhappy serf.

Additional References

A great deal of concrete evidence representing the points of view of the manufacturer may be found in the *Hearings before the Fed. Trade Commission*, 1917. *Women's Wear*, issues of Oct. and Nov., 1917, gives fairly good reports. The testimony of W. H. Ingersoll, H. C. Brown, and Sidney M. Colgate may be regarded as typical.

The points of view of retailers and consumers are exhibited in great detail in the *Hearings before the Committee on Interstate and Foreign Commerce of the House of Representatives.* Of these hearings there are three reports, (1) Feb. 27, 1914 to Jan. 9, 1915; (2) May 30 to June 1, 1916; (3) Jan. 5 to Jan. 11, 1917.

In report (1) see pp. 120 to 139 for points of view of manufacturer. In report (3) the points of view of both the Homemakers' Ass'n of New Jersey and the National Housewives League are given, pp. 97-108. In pp. 283-85 may be found the testimony of Miss Mary Wood representing the New York State and New York City Federations of Women's Clubs. The interests of retailers and consumers are discussed by Mr. E. L. Howe, Sec. of the Nat'l Retail Dry Goods Ass'n, in pp. 287-310.

In report (3) the retailers' point of view is also presented by H. S. Shelton, Pres. Ohio Retail Dry Goods Ass'n; V. W. Sincere, Gen'l Manager of the Bailey Co., Cleveland; P. S. Straus of Macy & Co.; E. M. Clark, Pres. of the Clark Bros. Stores, Scranton.

The wholesaler's point of view is given by N. H. Johnson, Sec. Southern Wholesale Dry Goods Ass'n.

CHAPTER VIII

The Middle Ground

To the reader it should now be clear that in the principle of price maintenance lurk great dangers, and at the same time some good features which if wisely applied would be of advantage to all parties concerned in the distributive system from the manufacturer to the consumer.

The commonly advocated form of price maintenance by allowing the manufacturer the option of compelling adherence to a standard price would in effect create a condition of general price uniformity. Such a condition would be, in the first place, entirely out of harmony with the fact that different retailers even in the same locality have widely differing costs of operation. It fails to recognize that retailers are not the same in business ability, nor are their business opportunities the same. And reliable data go to show that cost variations resulting from such dissimilarities are not confined within narrow limits, but extend to extremely wide ones—from less than ten per cent to thirty per cent of sales.[1]

Secondly, with respect to service involved in retailing, price maintenance fails to take note of the fact that some stores are forced by their clientele to furnish prompt and expensive delivery service, to give extensive credit accommodations, and to provide costly and elaborate quarters and apparatus for the gratification of their customers. Obviously such stores should be allowed a higher price than

[1] See *supra*, p. 54 *et seq.*

the unpretentious establishment in poor and meagre quarters, affording no accommodations whatever, by way of credit, or delivery or floor service.

Thirdly, the uniform price would require the assumption by the manufacturer of transportation charges on all outgoing goods. Such practice is already familiar, and with respect to certain classes of commodities whose transportation charges are a relatively small item, it is not objectionable. In connection with heavy goods, however, upon which transportation charges are relatively large and subject to rapid increase with length of haul, it is often desirable to shift the burden upon the distant dealer or consumer. This is especially desirable when the absorption by the manufacturer's overhead of the long-distance selling and transportation charges would necessitate a general price increase throughout the market. Price maintenance would prevent it.

From these objections we must draw the conclusion that any scheme of price maintenance, to be acceptable and just, must have the quality of *flexibility*. It must of necessity allow for price variations as costs vary.[1] The only safe basis of price-fixing of the wide and comprehensive type urged by the price-maintenance supporters is the cost basis. In the case of trade-marked and branded goods this is especially true because in connection with them a purely competitive price is but rarely possible. Brands or trademarks as a rule have the effect of setting apart the goods to which they are affixed, so that direct comparison between them and potentially competitive goods becomes very diffi-

[1] *Cf.* Statement of Mr. J. M. Barnes, credit manager of Marshal Field & Co. He argues for the maintenance of a system whereby retailers may fix prices on the basis of their varying costs. See *Hearings before the Interstate and Foreign Commerce Committee*, Jan. 5-11, 1917, pp. 79-90.

cult for the average consumer. Where a vestige of such a condition exists the consumer will buy more in response to an effective sales policy than out of a comparative knowledge of the merits of the commodity he is purchasing. In such case what he pays flavors more of monopoly price than of competitive price. The manufacturer is one step further removed from the necessity of making his price schedules conform with the expenses of production.

By certain defenders of price maintenance it is asserted that this flexibility is permitted by the Stevens Bill, which provides for the fixing of prices at the option of the manufacturer. It purposes to create a system whereby price maintenance may be enforced only through special contract between manufacturer and dealer, such contract to be entered into at the option of the manufacturer. It is true that flexibility of a certain type would result from this, but would such flexibility be used for any other purpose than that of increasing manufacturer's profits? Would not its pliability be utilized merely for local price-cutting to meet temporary competition—wholly indifferent to all consideration of cost variation in retailing? Few are the cases where the manufacturer is agreeable to price reduction by the dealer on the ground that the dealer has a low cost of operating. The granting of such a privilege to one would be tantamount to giving him a highly favored position above his competitors of the same class. The manufacturer thereby would not only lose much patronage from the other stores, but also incur their ill-will. Eventually the favored retailer would probably have no occasion to continue the cut prices, competition having disappeared, and consequently prices would be raised to the former level. This might be done without any loss of profit to the retailer, for his increased margin of profit per unit would perhaps more than offset the possible decreasing number of sales. The manufacturer

would not be so fortunate. His profits would fall in direct ratio with the volume of sales and orders from the other retailers would be lacking, unless all were assured equal treatment for the future.

So it is not to be expected that price reductions under the optional system would occur, except locally under the stress of competition between the manufacturers themselves. In this event local price cuttings and discriminations would be abundant. They would serve, however, merely as temporary instruments of competition. The history of the Standard Oil Co. and of the American Tobacco Co.—not to mention others—may again be referred to as illustrating just what would occur. They prove conclusively that in unfair competition no weapon is more vicious or deadly than that of local price manipulation to meet the competition of smaller companies. Such manipulation, if successful, is one of the surest ways of attaining monopoly.[1] It is not, we think, the wish of the American people to reestablish a system so replete with possibilities of evil as were formerly those of the two companies mentioned. The optional provision in price maintenance would probably accomplish this result.

Hence it cannot be said that the optional element in price maintenance, from the standpoint of public policy, is more desirable than the universality and uniformity of the more rigid system.

A fourth objection to be lodged against the present price-maintenance program is that it donates to the manufacturers all powers for restricting the distributors, but fails to provide for any restriction for the manufacturers themselves. Now, it is a poor rule that does not work both ways. Not yet can it be said that all virtue resides in the manufacturer

[1] *Journal of Commerce*, Dec. 6, 1915, p. 13, "Is a Food Trust Developing?"

and all vice in the dealer. Manufacturers themselves are often just as much at fault for the present price-cutting practices as the dealers. One of the greatest incentives to price-cutting is the granting of unreasonable quantity discounts to the large buyers. These discounts are often so great as to enable the large buyer to sell profitably at a price which represents the cost figure for the small buyer. The granting of excessive rebates for large sales is also a common practice.

The proposed scheme provides that the manufacturer shall at his pleasure change prices, the only requirement being that he file with the Federal Trade Commission his new price-lists and pay a nominal fee. Such changes can be made without conference with the dealers. If we suppose that the dealers are heavily stocked with goods for which they have paid a stated price, they would be put at a great disadvantage by an arbitrary cut on the part of the manufacturer,[1] or unduly favored by an arbitrary raise.

The dealer by the terms of the bill is allowed, under special contract approved by the manufacturer, to have special seasonal or disposal sales, say twice a year, or quarterly.[2] But such sales are allowed only when provided for in the sale contract.[3] If the dealer meets with any untoward incident, as bankruptcy or fire, or decides to withdraw from business, or by any other contingency is confronted with the necessity of liquidating his stock, he cannot do so until he has complied with the following provisions, involving much "red tape," and a minimum of thirty days loss of time:

[1] *Journal of Commerce*, March 11, 1916, "Broadside against the Stevens Bill."

[2] *Journal of Commerce*, Apr. 8, 1916; editorial.

[3] *Women's Wear*, March 21, 1916: "Barnet on Stevens Bill."

(c) Such contracts for the sale of such article or articles of commerce may provide for disposal sales at appropriate times, during which periods, duly set forth in such statement or in such schedule of prices as shall be filed by such vendor, such dealers may sell such article or articles of commerce for a price other than the uniform price as set forth in the schedule, provided in the preceding paragraph (b): provided, That such article or articles of commerce shall have first been offered to the vendor by such dealer, by written offer, at the price paid for the same by such dealer, and that such vendor not less than thirty days prior to the date set forth for the next disposal sale, after reasonable opportunity to inspect such article or articles, shall have refused or neglected such offer.

(d) Any article of commerce or any carton, package, or other receptacle inclosing an article or articles of commerce covered by such contract, and in the possession of a dealer, may be sold for a price other than the uniform price for resale by such dealer for such quality and quantity as set forth in the schedule provided in the preceding paragraph (b): First, if such dealer shall decide to discontinue the sale of such articles or article of commerce, or if such dealer shall cease to do business and the sale is made in the course of winding up the business of such dealer, or if such dealer shall have become bankrupt or a receiver of the business of such dealer shall have been appointed: Provided (a) that such article or articles of commerce shall have first been offered to the vendor thereof by such dealer or the legal representative of such dealer by written offer, at the price paid for the same by such dealer, and that such vendor after reasonable opportunity to inspect such article or articles, shall have refused or neglected to accept such offer: Provided, (b) That such dealer, or the legal representative of such dealer, shall file at the office of the Federal Trade Commission a statement setting forth the reason for such sale, the refusal or neglect of such vendor to accept such offer, and the grade, quality, and quantity of such article, or articles of commerce to be so sold; or, second, if such article of commerce or contents of such carton, package, or other receptacle shall have become

damaged, deteriorated, or soiled: Provided, that such damaged, deteriorated, or soiled article shall have first been offered to the vendor by such dealer by written offer, at the price paid for the same by such dealer, or at the option of such vendor, in exchange for similar articles not damaged, deteriorated, or soiled, and that such vendor after reasonable opportunity to inspect such article or articles shall have refused or neglected to accept such offer, and that such damaged, deteriorated, or soiled article shall thereafter only be offered for sale by such dealer with prominent notice to the purchaser that such article is damaged, deteriorated, or soiled, and that the price thereof is reduced because of such damage.[1]

The partiality of such a scheme is too obvious to require further emphasizing. Think of the country's million or more retailers, together with all its wholesalers and jobbers, bound up by such adamantine requirements, free to do nothing but act as puppets to the infallible oligarchy above them!

This suggests an additional conclusion, namely, that an acceptable form of price maintenance must impose upon the manufacturer restrictions consonant with those imposed upon the dealers. The dealer should at all times be guaranteed a fair margin of gross profit, and no dealer should be unduly favored over others by the giving of special rebates or discounts.

The fifth general objection to the uniform price arises from the power which it affords the manufacturer or his sales agent to attain without merit a position of virtual monopoly as regards the goods under his control. Supporters of price maintenance attempt to meet this argument with the claim that all specialty manufacturers would continue to meet competition, that the rivalry between brands

[1] Portion of Stevens-Ashurst bill now before Congress, H. R. 13568, 64th Congress, 2d Session.

and types is a matter entirely independent of price questions. "Why," say they, "should competition between Ivory Soap and Fairy Soap be any the less even with price maintenance imposed on both brands?" The reply is that there is in the scheme of price maintenance nothing inherently opposed to competition between manufacturers; but admission of this point does not refute the equally evident fact that price maintenance, while not preventing competition, does create conditions which discourage competition. Placing unquestioned responsibility in the manufacturer to fix not only his price to the jobber, but the price to the retailer and the consumer would so simplify the attainment of a combination or agreement that a mere oral agreement of a most informal nature between two or three men would suffice for its realization. Moreover, the motive for such an agreement between powerful competitors would be ever present. To place this motive within such easy reach of the means for its satisfaction is undesirable. Such is the conclusion to which we are led by the evidence of history, together with a consideration of the well-known characteristics of human nature as it actually exists.

In the previous pages there has also been noted the unmerited advantage over the rising young competitor which the old-established manufacturer would possess by virtue of price maintenance, in that this new power used in conjunction with practically unlimited national advertising would be almost competition-proof, price maintenance serving as a whip to keep all dealers in line and national advertising serving as a force to keep in well-defined channels the consumer's demand.

These considerations indicate that a defensible form of price maintenance must be not only flexible to conform to the varied retailing conditions as well as impartial in its treatment of both manufacturer and dealer, but also un-

availing for use as an instrument toward the building of monopoly either directly or indirectly.[1]

This condemnation of uniform price maintenance should not be taken as a defense by implication of the present system. Reversion to the descriptions of predatory price-cutting as offered in the previous pages calls to mind most vividly the resultant evils of that practice. For the below-cost type of price-cutting, in the absence of certain extenuating and very exceptional circumstances, there can be no valid defense. But with respect to the other type of price-cutting, we have already seen that our conclusions must be different. The retailing of a branded commodity by any number of stores at prices varying downward from the normal should be productive of no injury to the retailers themselves, to the commodity or to the manufacturer, provided each and every retailer makes a reasonable profit on the transaction. Recognition of this provision relative to reasonable profits would prevent the appearance of any desire on the part of retailers to discontinue handling the goods subject to price-cutting, hence the goods would suffer no unpopularity on the market, no unfavorable reaction would reach the manufacturer, and his price to the dealer as well as the quality of the good need not be affected. Excepting only a few incompetents who are always found on the margin, all the factors would profit from the practice as a result of increased demand and consequent more rapid turn-over.

This consideration introduces the solution of the price-maintenance problem here advocated. Unqualified price maintenance is unacceptable as is unlimited price-cutting, because both are devoid of checks and balances. Each gives to one set of individuals powers that are well-nigh absolute, while refusing to another set of individuals

[1] *Cf.* H. R. Tosdal, "Price Maintenance," *Am. Ec. Rev.*, vol. viii, p. 295.

who are just as vitally concerned all powers whatever. Price maintenance makes the manufacturer all-powerful, the dealer all but helpless; unrestricted price-cutting makes the dealer all-powerful, leaving the manufacturer all but helpless. Neither system possesses equilibrium. But a combination of the systems will secure equilibrium. The two extremes can be made to balance each other. This can be brought about by the adoption in retailing of the principle of a fair profit, as a criterion for price-making. If price-cutting can be accomplished by any dealer as a regular course of action, without forfeiting a reasonable profit on the goods whose prices are cut, and if such price-cutting is done openly and competitively, without misrepresentation or intent to deceive, such action must be regarded as being both ethically and economically correct. Such dealers as he are not only highly desirable, but indispensable to any industrial system which is not absolutely ossified.

But the question arises, how is the justifiable price-cutter to be distinguished from the predatory price-cutter? If the criterion be a fair profit, the distinction becomes possible. Such distinctions are now being made with great frequency and accuracy in virtually all of the great nations. Going back to a period prior to the Great War we find approximately similar problems being attacked with success by the Interstate Commerce Commission, the various State Public Utility Commissions, the Minimum Wage Boards, and, more recently, the Federal Trade Commission — to speak only of this country.

In brief, our plan is this: let the manufacturers, as at present, formally establish their standard uniform price for resale; let such dealers as wish to do so adhere to this price; let those who, by reason of economies derived from any source whatever, desire to cut the price, do so at their own pleasure, provided that they still retain a fair profit in

the commodity cut. Such action as has been shown in a previous chapter is without evil results, so long as all dealers are held to the same conduct. If no dealer is allowed to sell below the fair-profit margin, the situation becomes, from the competitive viewpoint, an ideal one. Every incentive is afforded for cost reductions and highest possible business efficiency. Each retailer can fix his prices to suit his own peculiar conditions. If he is serving a well-to-do clientele in a fashionable residence district, and is compelled to give elaborate service in the form of credit accommodations, special deliveries, etc., he is free to charge the maximum prices. If, on the other hand, he is doing business on some obscure side street where the customers belong to the poorer classes, where rents are low, where no accommodations are asked or given, where expenses of all sorts are at a minimum, he is free to charge the minimum prices, and rightly so. Such a system can be open to no objection, except the possible one of impracticability of enforcement. We think that this objection is not insurmountable. To be sure, in view of the extremely variant conditions which exist in the marketing system and which promise to become even more diversified in the future, no law can be constructed which provides in detail for every possible emergency. This necessitates the use of an administrative body with powers of discretion. Some of the difficulties to be overcome would be the following.

Both the costs and the economies of operation, though easy enough to measure for a business as a whole, are often extremely difficult to arrive at with respect to a particular unit of the business. A dealer who handles a varied line of goods knows that some of them have a rapid turn-over and that others move slowly; that some require much shelf or storage space, careful handling or assorting, and are particularly subject to the hazards of business, while other

goods have none of these disadvantages. In such case the proposed plan would call for the proper apportionment of the overhead to different classes of goods. Evidently he should have a greater margin of profit on slow-moving or easily-perishable commodities than on goods rapidly and easily moved.

Or again let us assume that as between two competing dealers we find a great similarity of stocks but a great difference as regards their apportionment or ordering. Say that one dealer has a stock one-third of which is the slow-moving type, while the other has a stock two-thirds of which, generally speaking, is slow-moving. At the end of the year their net profits may be the same, but their operating costs will be different. Here again we find that general costs offer no criteria for the pricing of specific commodities. Evidently, then, a classification must be made of commodities, grouping together those which bear approximately the same selling costs.[1]

To anticipate still another contingency, let it be assumed that a given dealer has been properly classified in respect to the rapidity of turnover and cost of handling the different classes of goods in his stock. This would entitle him to the privilege of fixing his retail prices on branded goods at any desirable point above a prescribed minimum. Let us suppose that an unexpected event then happens, such as the establishment of a new subway station at the door. This causes a doubling of the dealer's volume of business without any appreciable increase of overhead. Obviously the percentage of cost is radically changed and he becomes entitled to new limitations in his price-making.

Or again, let it be assumed that the given dealer having been classified according to the above suggestions, comes to

[1] *Cf.* Nystrom, *Retail Store Management,* Chicago, 1916, p. 76.

believe that by a cut in price below his allowed limit he can so increase his turn-over that the resultant decrease in percentage of cost will entitle him to a new classification which will act retroactively to legalize the previous radical cut. In other words, should the cut price be used as a cause in the endeavor to secure a more rapid turn-over and consequent less cost of operation, or should it come into existence only as a result of economies already attained, say in wise buying, ordering of stock, and superior selling methods? Obviously only the latter alternative is permissible, if we are to be consistent with the principle laid down. The use of the former might easily be attended by so many abuses as to make it no different from the present system.

A more difficult case to provide for arises where an enterprise in order to increase turn-overs offers special inducements other than price-cutting which serve to increase the general expense percentage. However, despite this increase in the percentage of cost, the net profits are enlarged in still greater proportion. Such procedure is not uneconomic, and no reason seems visible for discouraging its use by imposing upon it higher price-limits.

More contingencies could be mentioned, but these are sufficient to suggest that any plan on the order of the one proposed should be executed by administrative bodies which possess wide discretionary powers and the ability wisely to apply them.[1] Operating costs apportioned to classes of goods could constitute only the main criterion of price-cutting justification. Net profits should always be an additional guide, and no formula should be so inelastic as to fail to provide for all reasonable emergencies. It would require an elaborate or complicated machinery for its en-

[1] *Annals of the American Academy of Pol. and Soc. Sci.*, March, 1919, "The Advantage of Preventing Unfair Competition through an Administrative Body," W. H. S. Stevens.

forcement. Adequate standards and criteria could be worked out by a committee of experts, and adherence to them could be effected by any one reasonably familiar with business methods and accounting.

With the degree to which any given dealer may cut standard prices thus dependent upon the degree of economy which he achieves in his business, the question of accounting is given a new importance. A fair and scientific application of the principle proposed would probably require the establishment of a uniform system of accounting for those dealers desirous of cutting prices. Such an innovation is entirely practicable and would be justified by the accomplishment of salutary results other than those discussed.[1] Much of the inefficiency among dealers and much of the consequent increased cost of marketing are to be attributed to slothful and improper methods of accounting. A standard form of accounting properly adhered to and audited would have a twofold justification. It would encourage and make possible greater efficiency in business and would constitute a fairly trustworthy and simple means of distinguishing between the so-called predatory price-cutter and the profit-taking price-cutter.

Such a solution of the price-maintenance problem is not unlike that achieved by the Interstate Commerce Commission in the matter of regulating freight rates. The difference is one of degree chiefly, and is decidedly in favor of the former of the two tasks. The conditions which the proposed solution has to deal with are certainly far less diversified and dynamic than those within the scope of the Clayton Act and the Federal Trade Commission Act. The latter have to do with all the business forms and methods within our industrial system. The former contemplates

[1] Nystrom, *Retail Store Management*, pp. 74-84.

only one business form, the dealer, and only those practices accessory to this one form. The work heretofore of the Federal Trade Commission and of the Federal food boards in the matter of commodity price regulation should not be regarded as being exactly similar to that proposed. Their work was of the emergency type, and aimed only to prevent excessive profiteering while at the same time encouraging production. There was neither time nor occasion for the application of a scientific program such as we advocate, even had the machinery for it been available.[1]

Be it borne in mind, moreover, that the task here proposed differs from those above mentoned in this still greater respect: that it does not call for price-fixing at all. It calls only for the determination of *minimum limits* to price-cutting on such goods as have already received a standing and a fairly accurate valuation in the market. Obviously such a task is far simpler than that of price-fixing, and its advocacy creates no inconsistency with what was said in a former chapter relative to government price control.

It should not be presumed that the proposed plan would need to be applied in actuality to all the country's dealers. Probably a great majority of them would never be affected by its operation. As a weapon designed solely to be used by the manufacturer in his defense, its use would be directed against only a comparatively small proportion of dealers. In the first place, a large proportion of dealers are indifferent to price-cutting, or do not practice it even under present conditions. These would not be affected by the proposed plan. In the second place, a large proportion of manufacturers are indifferent to or opposed to price maintenance. These would make no attempt to utilize the plan.

Only those dealers who are actually desirous of price-

[1] *Annual Report Federal Trade Commission*, 1918.

cutting and whose manufacturers are opposed to it would need to resort to the plan, or be in any way affected by it. Although they would probably constitute only a small proportion of the total number of dealers, yet they would be sufficiently numerous to permit of a cut-price store within the reach of virtually every family. Thus may their present benefits be retained. But even of greater value would be the assurance that in the coming years no improvement in the distributive system need be retarded by the presence of so unyielding an incubus as unmodified price maintenance.

Such a program calls for no investigation of any dealer and is in no respect inquisitorial in its workings, except in cases of contemplated price-cutting in opposition to a manufacturer. It need not necessitate the disclosure of business secrets, or any information which might react detrimentally upon the dealers. It would require no elaborate or complicated machinery for its enforcement. Being confined to one form of business only, its standards and criteria could be worked out by a committee of experts, and adherence to them could be effected by any one reasonably familiar with business methods and accounting.

The feasibility of the plan, so far as the uniform accounting feature is concerned, has already been recognized and approved by many business men of the country,[1] by the Federal Trade Commission, and certain business schools. The dry-goods manufacturers of the country, in their recent agitation for the open-price association, admitted the

[1] "One of the most promising movements for the elimination of cut-throat competition, particularly the kind that grows out of ignorance of what it costs to do business, is the movement among business organizations to teach all dealers how to compute the costs of doing business in their own stores and to get them to establish uniform accounting systems, so that results from various stores may be compared readily. Practically every retailers' association in the country is now working towards this end." (Nystrom, *Economics of Retailing*, p. 177.)

necessity of some system of uniform accounting, in order to make their plan effective. Henry P. Thompson, chairman of the Executive Committee of the National Association of Finishers of Cotton Fabrics, in regard to this point says:

In any Open-Price Association a comparison of prices ought of necessity to be based on a uniform system of costs. Otherwise comparisons are misleading. In many associations cooperation among members has resulted in the installation of a scientific system of cost accounting, supplanting the old methods of keeping costs of labor and material, which are not difficult to keep with absolute accuracy, but guessing as to a proper distribution of that elusive but vital factor of general expense. A modern scientific cost system can distribute that general expense factor with precision.

Probably one of the most fortunate results of the outgrowth of the open price system is the establishment of proper cost systems with all the corresponding benefits to both buyer and seller. The final result to the head of any business acting under the Open Price Association is that he has accurate data of his own costs; he has accurate statements of his competitors' prices; he has accurate statements of the conditions of trade stated in weekly output and work on hand. With this information at hand, he can base his future actions with more degree of accuracy than if his information is based on guesswork.[1]

This system of uniform accounting for manufacturers is far more complicated than one for retailers, yet Mr. Thompson is unqualifiedly urging its adoption.[2] The Federal Trade Commission, recognizing the importance of some such scheme as a possible aid to it in the performance of its duties, is making repeated efforts to secure from Con-

[1] *Journal of Commerce*, Jan. 4, 1916.

[2] *Cf.* "Uniform cost plan of Tri-State Jobbers" in *Journal of Commerce*, March 13, 1916.

gress the power to enforce the adoption of certain standard accounting methods by the various types of business in the country. The Harvard School of Business Administration has demonstrated not only the desirability, but also the practicability of such an innovation.[1] Various progressive manufacturers of the country are also actively engaged in bringing about the same end by a campaign of direct education among their patrons.[2]

Finally, there remains the consideration that such a system would be productive of untold good to the dealer as a whole and, as has been previously indicated, would open the way to numerous other reforms at present impossible of direct attainment.[3]

The active operation of such a program would make unnecessary additional price protection for the manufacturers, would eradicate the predatory price-cutters, would put retailing on a safer and sounder business basis, and last, but not least, would insure to the consumer at all times the advantages resultant from increasing efficiency and economy in any part of the distributive system.

In order that such a system might be made thoroughly feasible, and competitive in the truest sense of the term, certain trade practices now existent must be, to a large extent, restricted. One of the most important of these is the giving of excessive quantity discounts.[4] It is the boast of certain chains and department stores that they can obtain from the manufacturer at practically cost prices. These

[1] See *Journal of Commerce*, Rep't of Harvard's Business School work, Dec. 1, 1915. *Bulletins* of Harvard School of Business Administration, nos. 1 to 10.

[2] *Journal of Commerce*, Nov. 10, 1915.

[3] *Journal of Commerce*, Dec. 6, 1915, p. 13. "Value of Perpetual Inventory System."

[4] Nystrom, *Economics of Retailing*, ch. xvi.

boastings are often not based on fact; but nevertheless it is true that during times of extreme depression, when factories are running below normal capacity, they will often accept large orders from the chains and department stores at bare cost prices. This raises the question of the economic justification of such a practice. Where fluctuations in demand are of such a nature that at certain periods of a year or of a business cycle factories within a given industry are left virtually without orders, it would seem that artificial stimulation of orders by drastic price-discounting would be justifiable, especially where the nature of the business requires the continuation of heavy overhead charges and the preservation intact of the organization itself. The principle should not, however, be applied further than is absolutely necessary for self-preservation. At least a certain number of the marginal producers would probably be thrown out of business. Under these conditions, sales made at a figure lower than the normal may not be economically reprehensible. They are at any rate preferable to combination or conspiracy where governmental machinery for regulation is at all inadequate. If, then, manufacturers find it necessary and justifiable, on occasion, to sell at a substantial discount or else not sell at all, there would seem to exist no sound reason why the dealers should not pass a portion of their savings along to the consumer. At such times all dealers are privileged to take advantage of the situation and purchase at low prices. If any fail to do so from lack of foresight or available capital, the fault lies only with them. It is the logical consequence of economic weakness chargeable to no factor outside themselves.

No different situation is created so far as the justice of price maintenance is concerned when the manufacturer, totally apart from considerations of necessity, chooses to adopt as a regular selling policy the granting of large quan-

tity discounts to the large buyers, while charging the maximum to the smaller buyers. Such a practice, uneconomical in the first place, becomes also unethical when this same manufacturer attempts by various methods to compel large dealers and small dealers to sell at the same price. Such a manufacturer, in view of the fact that he himself discriminates, should be estopped from the privilege of requiring others not to discriminate when such a privilege is wholly in his own behalf. Consider the injustice in this instance, where a manufacturer sells an order of goods at $2.50 per case, net, to a large mail-order house, and the same goods at $3.00 per case, net, to a small specialty store, yet requiring the two dealers to resell at the same price. He is foolishly creating a situation whereby the policy of price maintenance which he advocates is made not only unjust but virtually impossible.[1]

Yet a well-guarded scientific application of the quantity principle, based strictly on economic grounds, is not objectionable to the system here advocated. As a matter of fact, it is necessary to the success of the large dealers in many cases. For instance, a buyer of foresight, in anticipation of a busy season, wishes to lay in a stock of unusual volume. But storing room must be provided for the goods, insurance paid, risks of losses from deterioration due to dampness, vermin, age, etc., or to a downward trend in the market, assumed; and, furthermore, the interest on this inactive capital must be considered. The justice of discounts based on these considerations cannot be denied. But this policy of modified price maintenance here advocated would be rather hostile to the granting of discounts or rebates on any other bases to or by any of the factors in distribution. Otherwise the ideal competitive situation which it demands would be seriously endangered.

[1] *Printer's Ink*, Dec. 20, 1917, pp. 88-92, "Quantity Discounts under Fire."

Such indirect methods of securing price maintenance as we have previously designated, namely, the withholding of rebates, the severance of business relations, resort to agents and commissions so-called, would not be necessary for the protection of the manufacturer should the scheme here advocated be adopted. Therefore their further practice should be discontinued and strictly prohibited. That any one should have the right to select his own customers and to reward them as he sees fit has in the past been an axiom in business practice, and is expressly endorsed by a clause in the Clayton Act. But even this time-honored business principle must be severely shaken, we think, as the time-honored belief in *laissez-faire* has been shaken. Those economic forces in which we have so long trusted for the insurance of a measure of justice in the industrial relations of men are more and more coming under the dominance of human forces. As the power of the individual and of groups of individuals continues to grow, society must establish new criteria of just behavior. Those evils which at present can come only from *combination* or from *conspiracy* may be destined soon to come from the *individual*. Why hesitate to meet the issue? Its solution lies in considerations of the public welfare, and of that alone. In the program here outlined with reference to price maintenance, these considerations alone have been the criteria.

CHAPTER IX

Indirect Price-Cutting [1]

Indirect price-cutting, as indicated in a former chapter,[2] consists in the use of coupons, trading stamps, premiums and cash discounts for quantity purchases or as a reward for compliance with special sale stipulations. Such devices for the stimulation of business are being applied in this country to an extent that is really phenomenal, and now present one of the biggest problems in connection with the retailing business.

The premium idea, though in itself old, has come into general use in this country since the Civil War. B. T. Babbitt & Co., soap manufacturers, are credited with the first wide application of the idea through a highly organized premium system.

About 1885 the coupon system began to assume proportions which made it an imposing factor in merchandising. So rapid has been its growth that, according to recent estimates, merchandise premiums to the value of $125,000,000 annually are distributed in redemption of trading stamps and coupons, exclusive of the slips which are redeemed in cash or other methods. On this basis it is calculated that premiums figure in the selling of five billion dollars' worth

[1] This Chapter is based chiefly on a long series of articles on trading stamps and premium-giving which appeared in the *New York Journal of Commerce* and *Commercial Tribune*, and which were written for the most part by Mr. D. S. Kennedy lately of the editorial staff of that paper.

[2] *Supra*, p. 32, *et seq.*

of merchandise annually. It is also calculated that of the 20,000,000 families in the United States, 10,000,000 are redeeming coupons, through some member of the families or through the servants who handle the family groceries.

While these estimates cannot be relied upon for strict accuracy, they probably approximate the truth and demonstrate undeniably that the coupon is a powerful factor in modern retail trade. Its continuance or suppression is a matter of serious consequence.

To test the popularity of the coupon system, a house-to-house canvas was made in 1913 by trained investigators, with the following result:

Houses visited numbered 13,672. Of these, 2,974 were reported "not at home," 5,144 were not collecting coupons, 5,671 were collecting coupons. This amounted in Pittsburgh to an average of about 51% in favor of collecting premiums. Since the figures were taken, the proportion is believed to have increased. In Scranton, Pa., the average was 55% in favor of collecting; in Columbus, Ohio, the average was 37%; in Cincinnati, Ohio, the average was 70%.

Counting all trading-stamp companies, there are 35 or 40 in the United States, of which the more important are the following: the Sperry & Hutchinson Corporation of New York; the McKelvey Co. of New York; the Legal Stamp Co. of Boston; the Crown Stamp Co. of Philadelphia; the Eagle Stamp Co. of St. Louis and Cleveland; the Fish Stamp Co. of Chicago; the Brown Stamp Co. of Pittsburgh; the United Sales Corporation of Chicago; the Surety Trading Stamp Co. of New York.

There are approximately 65,800 retail stores in the United States using this means of sales stimulation. Pennsylvania leads the list with 13,500; New York is second with 11,500. It has been estimated that less than 25% of

all grocers, exclusive of chain stores, distribute the coupons of large central companies. The chain stores, however, are strong advocates of the system. The coupon system has been found more difficult to fight because actual trial has demonstrated that it is impossible to boycott goods with which coupons are packed.

The Larkin Co. was established in 1875 and adopted the premium plan about ten years later. The business of the company has grown steadily and rapidly until now it has reached the point where it claims to have more than 2,000,000 customers. A special feature of the Larkin premium system is "the club of ten" plan. This induces women to organize clubs of ten members, each of whom subscribes one dollar a month for ten months, and each of whom receives in rotation a ten-dollar premium. It has been stated that some of the women who have made a business of organizing these clubs have as many as thirty-five going at a time, and send in on an average $6,000 annually.

The American Tobacco Co. has said that only about 40 or 50 per cent of its premium-value coupons are redeemed, but that 98 per cent of the cash-value coupons are turned in for redemption. At present the metropolitan district of New York is the best field in the country for condensed milk premiums, more than 80 per cent of the labels being redeemed here. In 1913 the Wisconsin Condensed Milk Co. redeemed 21,000,000 labels and coupons. It is estimated that from 75 to 90 per cent of laundry soap wrappers are redeemed annually. The soap concerns using the premium plan divide into three classes as to size of business:

1. Firms spending $250,000 annually in premiums—Colgate Company.

2. Firms spending $150,000 annually in premiums—Proctor & Gamble; B. T. Babbitt Co.; Kirkman & Son.

3. Firms spending $100,000 annually in premiums—Kirk Co.; Lautz Co.; B. J. Johnson; Globe Co.

The United Cigar Stores Co. in 1913 spent about $2,000,000 in advertising, of which $80,000 was spent for space in newspapers. This company issued 800,000,000 coupons. The expenditures of the Liggett & Myers Tobacco Co. for premiums in 1913 reached two and one-half millions.

The use of coupons and trading stamps may be classified under three heads, within which there are numerous ramifications. They are:

First. The trading stamp which is issued by the merchant himself and is redeemed by him in cash or merchandise. In this case the transaction is entirely between the retailer and consumer. It is a local business and no questions of interstate commerce can intrude.

Second. The trading stamp issued to the retailer by a company which has specialized in the business. The latter concern has a premium slip printed, of a distinctive color and name, which is sold to the retailers in all parts of the country at a definite sum per thousand. The consumer gets the stamps, together with a catalogue from which he may select a number of premiums, redeemable for a stated figure in slips. Usually the stamps are also redeemable in cash at about one-half of their face value in merchandise. The transaction, after the stamp has passed to the consumer, is entirely between the original company and the purchaser. One of the largest concerns engaged in this business is the Sperry & Hutchinson Corporation of New York, which sells the Green Trading Stamp.

Third. The coupon issued by the manufacturer with his goods. In this instance the premium slip is usually packed with the articles themselves or forms part of the wrapper. The consumer automatically receives his coupon with the

package, and any further transaction is carried on with the manufacturer. This is a frequent accompaniment of trade-marked and nationally advertised products. The use of the coupons is intimately connected with the price-maintenance problem which is now before Congress, and over which the mercantile world is now fighting.

The second system outlined above may be divided into two classifications: the selling of coupons to retailers for distribution, and the selling to manufacturers for incorporation in their packages. The largest concern in the second field is the United Profit Sharing Corporation of New York, which sells its coupons only to manufacturers, and then only to one manufacturer in one line, thus giving a feature of exclusiveness to its patronage. This company issues the coupon used by the United Cigar Stores Co. and is largely controlled by the latter company.

Within the limits of these three fundamental divisions the name of the coupon tribe is legion. Beginning with the coupon which is redeemable simply in cash or in merchandise, the uses and lures of the system are being constantly augmented. New schemes appear almost daily. Among the most extreme is the Travel Coupon, a magnificent document which carries on its face the pictures of speeding express trains and palatial liners. The purchaser is told that this system, paying four per cent return on his living expenses of $1,000 a year, will give him the total of $40.00, with which he can take his wife and daughter to the seashore or, if he is thrifty for several years, can plan for a trip to Europe.

Some large retailing corporations ostensibly opposed to the use of coupons, have, nevertheless, established trading-stamp plans of their own. The Macy Company extracts coupons sold by third-party companies to manufacturers.

but has a cash discount which in effect utilizes the principle of the trading stamp. Marshall Field & Co. have been known to distribute coupons of their own, while refusing to permit the use of other premium slips. In general, however, these companies have opposed the coupon system consistently, and have maintained their principles without serious deviation. The Macy Company allows its customers four per cent on cash deposited with it and at the end of the year returns to each customer two per cent of the amount expended with the store.

The argument of the coupon companies that the system is a form of advertising appears to be entirely fallacious. Justice McKenna of the United States Supreme Court has defined advertising as "merely identification, description, and apprising of quality and place, having no other object than to draw attention to the article to be sold." The statement that the coupon is advertising is a specious plea in self-defense. It does not acquaint the prospective purchaser with the nature or quality of the article. It does not inform him of the place where the article will be sold. It does not state the price of the merchandise or explain its merits above other articles of a similar character. In this respect, therefore, the coupon is not a legitimate competitor of the newspaper or the magazine, which carries to thousands of readers information which the coupon system cannot convey. The coupon depends upon a psychological element directly at variance with that of the newspaper, and grasps the customer only after the article has once been purchased. The incentive to buy a second time does not come because the coupon has convinced the purchaser that the article merits attention, but because of the value of the coupon itself, apart and distinct from the merchandise.

The coupon system is a form of price-cutting, and as such is inherently opposed to the principle of price maintenance.

The fact, however, that the plan is approved by many of the most pronounced advocates of price maintenance is proof that the coupon has a power above its value as a discount. There is no doubt that the average purchasers, and even those of more than ordinary intelligence, feel that they are obtaining in the coupon something that is in addition to the worth of the article they have bought.

The coupon makes it possible for the dealer to give a cash discount smaller than could be done in legal tender. It would be impossible to give to the purchaser of a five-cent cigar a discount of four per cent in any other manner than with the coupon. This system also eliminates the necessity of keeping credit accounts, which would be required to give to a customer at the end of a year a discount on his purchases. It places a premium on cash purchases by returning a percentage of the price not available to those buying on a credit basis. These are features in favor of the coupon system.

Upon looking more fully into the system, however, it must be strongly doubted if the evils of the plan do not greatly outweigh any advantages it may have. The cash discount in any store will stimulate trade temporarily, but at a tremendous cost. It is a form of competition that encroaches upon the capital of the enterprise, reducing dividends and sending up the expense charge. It is to be questioned whether competition that adds four per cent or even two per cent to the cost of doing business can be justified. If the retailer or the manufacturer passes on the expense to the consumer, the cash discount feature loses its character and the purchaser is paying directly for the additional value. The only vestige of the original theory which is left is that the purchaser carries in his mind the illusion that he is obtaining more than he has paid for. This in itself might prove of advantage to the retailer and increase his business

if it were not for the fact that, as every form of competition tends to draw others to its level, neighboring companies would likewise be drawn to the adoption of the coupon system. This would nuulify the value of the cash-discount plan.

Withe the operation of economic principles as outlined, the only beneficiaries of the coupon system are the companies which issue the premium slips and which divert to themselves the difference between the two per cent paid by the retailer and the four per cent paid by the consumer. Part of this profit, of course, is returned to the purchaser in the form of premiums; but the fact remains that the officials and employees of the coupon companies receive pay for which they have not rendered adequate service to mere merchandising. They impose upon the distribution of merchandise an added item which is unnecessary to its success.

The average retail grocer charges the purchaser approximately twenty per cent more than the cost of the merchandise. Of this twenty per cent, from seventeen to nineteen per cent is consumed in the cost of operation, leaving only a small margin as clear profit on each transaction. If he turns over his stock five times during a year he makes a profit of, say, from ten to fifteen per cent. If he adds to cost of operation two or three per cent as the cost of trading stamps, the number of turn-overs must be increased beyond all hope or expectation in order completely to offset this cost. In case he has competition in the use of the stamps, the chances are that he will find them veritable profit-killers. Either this must happen or a general increase in the consumer's price must follow.

Assuming, however, that the use of the coupon will increase the business of a concern considerably in the course of a year, as it appears to do when one company adopts it in advance of its competitors, we find that still another eco-

nomic factor comes into play. A large grocery distributor does an annual business of $10,000,000 upon which he makes a profit of ten per cent, or $1,000,000. He feels that the use of coupons will increase his trade by $2,000,000 a year, a substantial expansion. He tries the plan, and at the end of the year finds that he has succeeded in his expectation. But he also discovers that the cost of the coupons upon his entire turn-over of $12,000,000 at two per cent is $240,000. His profit on the additional $2,000,000 is $200,000, a clear loss of $40,000 in the year because of his adoption of the coupon system. In other words, although the effect of the use of stamps and coupons may be to increase the total volume of business, it may tend to swell the cost of operation at a still more rapid ratio.

An additional result of this adventure is that by the end of the year the grocer's competitors have met his cash discount competition by using trading stamps also. Consequently none of the retailers are benefited, while the consumer has experienced an increase in the cost of living or the retailer has been compelled to pocket the loss himself. The premium companies, on the other hand, have made profits not only in the ordinary sale of coupons, but also through the failure of purchasers to redeem their slips, a feature of considerable importance when it is recalled that this loss amounts to between two and fifty per cent of the entire stamp issue.

It has been discovered that when a community of merchants have committed themselves to the use of coupons, the eradication of the system is a matter of the utmost difficulty. The purchasers have become accustomed to the use of the stamps and cannot see readily that their withdrawal may ultimately result in a decreased cost of living, through the free play of competitive forces. Further than this, there is the opposition of the coupon companies themselves,

who invoke the provisions of the Sherman anti-trust law against any combination of merchants who combine to throw off the use of coupons simultaneously.

Such has been the experience of several organizations. The Chamber of Commerce of Providence, R. I., adopted a resolution condemning the use of coupons and urging its members to abandon the practice. The affair was taken up by the United Profit Sharing Corporation of New York, which threatened to bring suit for conspiracy in restraint of trade. The resolution was afterward withdrawn. Similar action was taken by a retail grocers' association of Chicago, with a like result.

The coupon system in another manner affects the problem of price maintenance, and in a way not approved by manufacturers. When redeemed by premium companies for merchandise, the coupons bear a higher value than they will bring in cash, because the coupon companies are able to purchase their supplies in large quantities at wholesale prices far below the retail charge. Two hundred and fifty coupons will be redeemed in cash for $2.50 but will secure a Gillette safety razor, the retail price of which is $5.00. In New York and other large cities coupons may be purchased at small shops, which are widely advertised, at $1.00 per hundred. It is possible accordingly for the prospective purchaser of almost any standard-priced article to buy it through the medium of coupons at about half price. This is a feature of price-cutting which reacts upon the manufacturers of identified goods and which they have not yet been able to neutralize.

Doubt is cast upon the value of the coupon system as a merchandising factor by the record of large stores in New York in the last several years. Of the seven great department stores which have gone into bankruptcy, all were patrons of the coupon plan. Opponents of the scheme have

asserted that the drain of the cost of coupons was a potent factor in their failure. Too much faith must not be put in the argument, but it undoubtedly has weight. One of the largest department stores in New York conducted an investigation in 1915 to test the price of articles sold by a neighboring department store of a similar character, but using coupons. This concern spent $62.50 in purchasing 25 or 30 articles from the coupon store. Advantage was taken of the periods of the day when the store gave the greatest values in coupons, as it was the practice to offer double stamps in the dull morning hours, and occasionally to give extra stamps with special sales. The coupons collected in this manner equaled the value usually obtained with $100.00 worth of merchandise. The coupons when redeemed secured one dozen spoons worth $2.00 retail. The store making the investigation accordingly obtained goods worth $64.50 at an expenditure of $62.50. But it was discovered that the same articles, manufactured by the same concerns, were sold for $56.35 in the store which did not use trading stamps, making a saving of more than four dollars by the purchase in the latter store.

An argument advanced by President Caldwell of the Sperry & Hutchinson Corporation is that the coupon plan is a form of profit-sharing, in which the customer receives a share of the income derived from his constancy in buying the articles which carry coupons. This plea would be valid if the coupon system were restricted to one store in a town or to one article in a store. It loses its strength in proportion to the growth of the coupon system.

In April of 1915 the New York *Journal of Commerce* sent inquiries to leading merchants in all of the larger cities of the country asking their opinions as to the use of coupons and trading stamps. With few exceptions, the replies indicated the feeling that the coupon system was bad econom-

ically and, in addition, extremely difficult to abandon when once adopted. The opinion prevailed that the coupon system in its wider aspects is a burden upon merchandising and increases the cost of living. It is not advertising and performs no useful function in that respect. At the same time it has gained a strong foothold, especially among consumers who are not accustomed to reason in economic terms, and a long struggle will be required to oust it by legislative force or by the education of consumers.

The struggle has begun, however. Several states have applied legislation in the fight against the coupon systems, notably Florida, Alabama and Washington. Much litigation has ensued. The courts of many of the states have held unconstitutional laws directly prohibiting the use of premium slips. The effect of these rulings has been nullified, however, so far as the Federal Constitution is concerned, by the recent decision of the United States Supreme Court, filed March 6, 1916. This is the only opinion of the Court in a suit involving trading stamps and coupons. The case was threefold, embracing appeals from the United States District Court for the Eastern District of Washington, an appeal in error to the Supreme Court of the State of Washington, and an appeal from the United States District Court of Florida. In each of the three the Court refused to hold that the laws of the several states, in effect prohibiting the coupon and trading-stamp business, were in violation of the Federal Constitution, with respect to the "due process clause," the "equal protection" clause, or the "interference with interstate commerce" clause.

Of the state statutes antagonistic to premium systems. that of the state of Florida seems to be the most effective. and, moreover, has received the sanction of the Supreme Court. The Florida statute was passed in 1913, imposing heavy license taxes and providing that merchants, druggists

and store-keepers shall pay a license tax upon the cash value of the stock of merchandise, amounting to $3.00 for the first $1,000 or fraction thereof, and $1.50 for each additional $1,000 or fraction thereof. The tax upon wholesale dealers is $1.50 upon each $1,000. But in the statute there is:

Provided further, that each and every person, firm, or corporation, who shall offer with merchandise bargained or sold in the course of trade, *any coupon, profit sharing certificate, or other evidence of liability redeemable in premiums, shall pay annually a State license tax of five hundred ($500.00) dollars, and a County license tax of two hundred and fifty ($250.00) dollars in each and every County in which said business is conducted or carried on*, and if more then one place of such business shall be operated by any person, firm, or corporation, a separate State and County license shall be taken out for each such place; and no person, firm or corporation shall offer with merchandise, bargained or sold as aforesaid, any coupon, profit-sharing certificate, or other evidence of indebtedness or liability, redeemable by any other person, firm, or corporation than the one offering the same, without paying the above license for each other person, firm, or corporation who may redeem the same. The license prescribed in this section shall be in addition to other licenses prescribed by this act. Any person violating any of the provisions of this section, whether acting for himself or as the agent of another, shall, on conviction thereof, be punished by fine of not exceeding one thousand dollars ($1,000), or by imprisonment in the County jail not exceeding six months.

Mercantile agencies shall pay a license tax of one hundred dollars in each county in which an office is established.

Merchants using trading stamps shall pay a license tax of two hundred and fifty ($250) dollars for each place of business where they use such stamps.

Certain Florida merchants, as was to be expected, brought suit to prevent the enforcement of this law.

The Court, as above indicated, found that dealing in coupons and trading stamps does not properly constitute interstate commerce. Hence it is a matter primarily of state concern, and the control of coupon and trading-stamp systems should be left to the legislatures. This decision constitutes the first important victory of the coupon opponents in the courts.

The decision of the Commissioner of Internal Revenue, W. H. Osborne, made in the early part of April, 1916, is a second blow to the progress of the coupon corporations. In the regulations of the Treasury Department governing the collection of the internal revenue is a provision that all packages of cigars, cigarettes, etc., in interstate commerce shall, if they bear coupons at all, bear them in like manner in all the states. For years this rule had been allowed to lapse. But Mr. Osborne now declares that he intends to enforce the regulation strictly. The effect of this order is that if one state prohibits the use of coupons, the prohibition also controls the issue of similar coupons in all the states.

Nevertheless, at present and in practically all of the states, three or four only being excepted, the activities of the coupon and trading-stamp companies are for the most part still free and unhampered by repressive legislation. Signs are unmistakable, however, that the opposition to them is setting in with a stronger force than ever. Discerning eyes cannot fail to see that such contrivances for the stimulation of trade are extremely superficial and only in isolated instances effective. In the long run it cannot fail to be other than an additional burden heaped upon a distributive system already tottering under a load of costs that seem both innumerable and superfluous.

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CHAPTER X

The Legal Status of Price Maintenance

Federal statutory law, with respect to price maintenance, has long been vague and indeterminate. Statutory law, both state and federal, has been inexact and not at all comprehensive. The Sherman Law of 1890 does not directly allude to it.[1] It will be noticed that it condemns contracts, combinations, monopolies and conspiracies in restraint of trade and commerce. No allowance is made, however, for considerations of patent and copyright monopolies, and the general vagueness of the terms as to both their meaning and their application has led the courts only to hopeless controversy.

The recent Clayton Act, although more specific in its description of illegal trade practices, does not by any means go to the root of the matter. The only provision which may be said to affect our problem is found in Sec. 3, which forbids only the use of the notorious " tying clauses " in contracts of sale—that is, no person may sell or lease goods to another under a contract or agreement preventing the latter from dealing in the goods of a third person. Even this provision is weakened by the qualification that it applies only where the " agreement or understanding may be to substantially lessen competition or tend to create a monopoly in any line of commerce." [2]

The Federal Trade Commission Act, with respect to price

[1] See Appendix, p. 198.

[2] See Appendix, p. 199.

maintenance, provides simply that unfair methods of competition shall be declared unlawful.

This marked inadequacy of legislation relative to price-fixing has been gradually offset by judicial expansion of the statutes. The state courts have been much in conflict in decisions regarding analogous cases and have in general refrained from formulating any definite or comprehensive rulings. Decisions of the federal courts, until recently, have not been of such a nature as to afford a basis for any safe generalization relative to the legality of price maintenance. Compelled to create a "rule of reason" by the Sherman Act, and again thrown back wholly upon their discretion by the Clayton and Federal Trade Commission Acts, the judiciary quite naturally was reluctant to make comprehensive rulings, and did so only under the pressure of relentless and very severe litigation extending over a period of more than a decade. Not until March, 1918, did the Supreme Court bring into clear relief its theories on this subject.

In line with the recent positive and conclusive attitude of the Supreme Court are the late activities of the Federal Trade Commission. Acting under the authorization of Sec. 5 of the Federal Trade Commission Act, this body during the past year, 1918, has been relentless in its investigation and condemnation of alleged price-maintenance cases. At this writing (Feb. 1919) there are pending before it no less than 27 such cases. At present its ruling seems to be thoroughly consonant with those of the Supreme Court; and nothing is now evident which warrants any expectation of a change in its policy.

Consequently, it may now be stated with assurance that the following methods of maintaining prices are illegal: (1) by notice affixed to the commodity or its wrapper, or printed thereon; (2) by special contract between manufac-

turer and dealer; (3) by any sort of license agreement whereby the dealer is technically classified as an agent, or whereby a sale is disguised as a consignment; (4) by threats to discontinue trade relations upon the failure to maintain prices, by intimidation of any sort, or by conspiracy with jobbers or dealers to withhold supplies from the offending price-cutter; (5) by the retention of rebates, or the refusal of discounts, upon the failure of the dealer to maintain prices; (6) by any type of conditional sale whereby the title of the goods fails to pass to the dealer except upon recognition of price-maintenance stipulations.

No special privileges or powers relative to price control seem to reside in patentees or their assignees or in the holders of copyrights. Apparently they are in the same category, with respect to resale price-fixing, as are the manufacturers or sales agents of proprietary or ordinary trade-marked commodities.

The successive steps of the federal courts in their approach to the present rulings are given herewith chronologically. To review all the cases would be superfluous, hence we have attempted to bring forward only those of most importance. We shall deal first with those in which patent rights are involved.

PRICE MAINTENANCE AND PATENT RIGHTS

The Heaton-Peninsular Button Fastener Co. was the holder by assignment of patents covering certain machines for fastening buttons on shoes.[1] The machines at that time were very successful in the market, 49,000 of them being in use, with practically no competition. The machines were made specifically to be used with a certain type of staple manufactured by the same company, and they also bore on a metallic plate the inscription:

[1] The Heaton-Peninsular Button Fastener Co. *vs.* Eureka Specialty Co., 77 F. R. 288, decided Oct. 12, 1896.

Conditions of Sale

This machine is sold and purchased to use only with fasteners made by the Peninsular Novelty Co. to whom title to said machine immediately reverts upon violation of the contract of sale.

The Court took the position that a patentee has exclusive monopoly rights in his invention and that the above condition was only a reasonable exercise of such rights. The Court's belief in the inviolability of patent rights is well illustrated by the following excerpt: the patentee,

if he see fit, may reserve to himself the exclusive use of his invention or discovery. If he will neither use his device, nor permit others to use it, he has but suppressed his own. That the grant is made upon the reasonable expectation that he will either put his invention to practical use, or permit others to avail themselves of it upon reasonable terms, is doubtless true. This expectation is based alone upon the supposition that the patentee's interest will induce him to use, or let others use, his invention. The public has retained no other security to enforce such expectations. A suppression can but endure for the life of the patent, and the disclosure he has made will enable all to enjoy the fruit of his genius. His title is exclusive, and so clearly within the constitutional provisions in respect of private property, that he is neither bound to use the discovery himself, nor permit others to use it.

So the rights of a patentee, by conditions of sale, to control the use of his article even after it has passed from him, and is in the hands of the vendee, is here unqualifiedly upheld, and the *dicta* of the Court are certainly not hostile to the idea of resale price maintenance.

The next case goes a step further, its main consideration being that of price control. But it will be noticed that the parties to the suit are licensor and licensee of a United

States patent. The attitude of the Court toward restraint of trade in its relation to patent monopoly is also well worth noticing.

The National Harrow Co. of New York [1] was the owner by assignment and purchase of a large number of United States letters patent covering inventions embodied in the "float spring tooth harrow." By special contracts based on valid consideration, the National Harrow Co. granted to the Bement Co. the license and privilege of using the rights under those patents in its business of manufacturing, marketing, and vending to others to be used, float spring tooth harrows and attachments. In the agreement between the two companies it was specified that Bement should allow no rebate or reduction from the price or prices fixed in the license. When the articles of contract were broken by Bement, the National Harrow Co. brought suit, and the case finally reached the United States Supreme Court. The defendants maintained that the contracts with plaintiff were illegal as being against public policy, and contrary to the spirit and letter of the United States Anti-Trust Act, the Sherman Law.

In a decision favorable to the plaintiff, the Court developed its argument somewhat as follows:

> . . . the general rule is absolute freedom in the use or sale of rights under the patent laws of the U. S. *The very object of these laws is monopoly,* and the rule is, with few exceptions, that any conditions which are not in their very nature illegal with regard to this kind of property, imposed by the patentee and agreed to by the licensee, for the right to manufacture or use or sell the article, will be upheld by the courts. The facts that the conditions in the contract *keep up the monopoly or fix prices does not render them illegal.*

[1] Bement *v.* National Harrow Co. (186 U. S. 70), decided May 10, 1902.

The Court admits that the contracts are in restraint of trade and commerce between the states, but holds that such restraint is not in violation of the Sherman Law, because it arises from reasonable and legal conditions *imposed by the owner of a patent.* Furthermore, the Court admits that the contract resulted in keeping up the prices of the commodities, but "*this the parties were legally entitled to do.* The owner of a patented article can, of course, charge such price as he may choose, and he may assign it or sell the right to manufacture and sell the article patented, *upon the condition that the assignee shall charge a certain amount for such articles.*"

In the next case the problem of resale price maintenance springs up before us in full blossom. Especial notice should be taken of the conditions of sale involved. The Court, it will be seen, is unqualified in its endorsement of resale price maintenance in this particular case.[1]

The Circuit Court of Appeals was faced with these facts: The Victor Talking Machine Co. sold to The Fair its talking machines with the notice affixed thereon that the use of the machine was granted only in case it sold for not less than $25.00, and that a less price meant an infringement of its patent rights. The Fair sold them for $18.00, and were thereupon sued for infringement. The Victor Co. was upheld, and the attitude of the Court is well expressed in the following excerpt from Judge Baker's decision:

The patent grant covers three separate or separable fields. The patentee may agree with one that he will not exclude him from making, with another from using, and with yet another from selling devices that exemplify the principles of his invention. . . . The field of sale is as much within the monopoly

[1] Victor Talking Machine Co. *vs.* The Fair (123 Fed. Rep. 424). Decided in 1903. "The Fair" alluded to is a large department store in Chicago.

as the others, *and so it has been decided* . . . the holdings were that a patentee may reserve to himself as an ungranted part of his monopoly of sale, *the right to fix and control the prices at which jobbers and dealers may sell the patented article to the public,* and that whoever without permission enters the reserved portion is an infringer.

The right to maintain prices on patented articles by an agreement entered into at the time of sale is also upheld in the case of the National Phonograph Co. *v.* Schlegel.[1]

The complainant in this case was the exclusive licensee for the sale of Edison phonographs and records. In 1901 it entered into a contract in writing called "jobbers' agreement" with defendants. The terms of the contract in the main were: (1) to sell only at certain named prices; (2) to sell to no retail dealers who do not sign a prescribed and similar agreement governing and controlling sales by retail dealers; (3) all Edison phonographs and records are sold under the condition that the license to use and vend them implied from such sale is dependent on the observance by the vendee of all the foregoing conditions. Upon the breach of any of them the license to use or vend the said phonographs and records immediately ceases, and any vendor or user thereafter becomes an infringer of said patents, and may be proceeded against by suit for injunction, or damages.

In its judgment the Court said:

In this case the exclusive right to sell has been transferred to complainant, and to that extent it controls the monopoly granted by the letters patent. An unconditional sale by the patentee, or by a licensee authorized to make such sale, of an article embodying the invention or discovery, passes the article without the limits of the monopoly, and authorizes the

[1] (128 F. R. 733). Decided March 10, 1904.

buyer to use or sell it without restriction; but to the extent that the sale is subject to the control of whoever retains the monopoly. . . . The condition against sales to retail dealers who do not sign a similar agreement governing sales by them was imposed by complainant in the legitimate exercise of its property right in the monopoly, and for the purpose of rendering it valuable. The complainant had the same right to require that such an agreement be exacted from defendant's vendees that it had to demand it from defendants. Any sale by defendants outside of the terms of their under license or contract was an invasion of complainant's lawful monopoly. The contract which the parties had made, and which defendants were violating, was a valid one.

Still further reinforcement is added to the cause of the patentee in his efforts to control the behavior of retailers in respect of prices in the famous Dick Case. Here, however, the right *to use*, and the right to *transfer the right to use* are of more importance than price considerations. Many are the times, though, when this case has been resorted to as a champion of price maintenance.[1]

The A. B. Dick Co. of Chicago, manufacturers of a rotary mimeograph, sold one of their machines to Miss Christina B. Skou. Upon the machine was inscribed the following notice:

LICENSE RESTRICTIONS

This machine is sold by the A. B. Dick Co. with the license restriction that it may be used only with the stencil paper, ink and other supplies made by the A. B. Dick Co., Chicago, Ill.

The defendant, Sidney Henry, sold to Miss Skou a can of ink suitable for use upon the mimeograph with knowl-

[1] Henry *v.* Dick Co. Decided March 12, 1912, in the U. S. Supreme Court, 224 U. S. 1.

edge of the said license agreement, and with the expectation that it would be used in connection with said mimeograph. The ink sold to Miss Skou was not covered by the claim of the mimeograph patent. Whereupon the Dick Co. brought suit, alleging that the use of this ink with their patented mimeograph was an infringement of the patent rights.

The Court in its decision, written by Justice Lurton, declared for the complainants. It unqualifiedly held that the broad and general statutory rights of a patentee to make, use and vend the article containing or embodying his invention, privileged him lawfully to restrict others as to the manufacture, use and sale of the article. Such restrictions were in the nature of a conditional sale, the purchaser buying the goods with knowledge of the restrictions. Where the restrictions were not mentioned in the sale, the patentee possessed no rights as to the future disposition of the goods. With respect to this last idea, the Court argued as follows:

An absolute and unconditional sale operates to pass the patented thing outside the boundaries of the patent, because such a sale implies that the patentee consents that the purchaser may use the machine so long as its identity is preserved. This implication arises, first, because a sale without reservation of a machine whose value consists in its use, for a consideration, carries with it the presumption that the right to use the particular machine is to pass with it.

As to the kind of limitation which may be lawfully imposed upon the purchaser, the Court said:

"To begin with, the purchaser *must have notice* that he buys with only a qualified right of use."

In parting with his right the patentee seemingly would have a very broad freedom, for the Court quotes approvingly from the case of Bement *v.* National Harrow Co.[1]

[1] *Supra*, p. 160.

Now price maintenance was not directly involved in the Dick Case. Yet the majority of the Court was so firmly of the opinion that the right of price control under a license agreement inhered in the patentee, that it quotes freely from other decisions which approve price control to support it by analogy in its main conclusion, namely, that the patentee has the right to control *the use* of his article under a license agreement, and that violation of any such restrictions constitutes an infringement of the patent rights.

The development of rulings favorable to price restrictions imposed by patentees received a rude jolt in the case next to be considered. The reader's attention is called to the manner in which the Court evades the rulings previously laid down, especially that of the Dick Case. It will be noted, too, that the Court takes a new and entirely different attitude in its reasoning on monopoly and restraint of trade. As an important technicality, there comes to the front also the part which royalties have to play in price-maintenance arrangements.[1]

The Waltham Watch Co. was the holder of certain patents covering inventions embodied in the watch movements manufactured by the same company. Assuming that the letters patent empowered such action, the Waltham Watch Co. in all its sales of watch movements injected certain stipulations and notices to the effect that dealers, both retail and wholesale, should maintain the prices fixed by the company, and that any failure so to maintain the prices would revest in the company the title of the movements. The Court held that these conditions of sale were null and void. The Dick Case, it said, does not apply, because in that case the manufacturer sold his machines at cost, depending for

[1] Waltham Watch Co. *v.* Keene (202 F. R. 225). Decided Feb. 13, 1913.

his profits upon the sale of accessories for the machine—in short, *did not receive full consideration for the sale of his machine at the time of sale.* In the Waltham case, however, the conditions are entirely different, says the Court in effect. The manufacturer received *full compensation* for his articles *upon their first sale.* This leads the Court to quote approvingly from Adams *v.* Burke (17 Wall. 453), as follows:

> . . . The patentee or his assignee, *having in the act of sale received all the royalty or consideration which he claims* for the use of his invention in that particular machine or instrument, *it is open to the use of the purchaser without further restriction* on account of the monopoly of the patentee. And this does not do the patentee or his assignee injustice, because " it does not deprive a patentee of his just rights, as no article can be unfettered from the claim of his monopoly *without paying its tribute.*" In this case the articles had paid their full tribute, and hence no restriction could properly be attached to them. The Court suggests: " That a patentee *may create selling agencies* and control the price goes without saying; but *once sold and the royalty received by the patentee,* the patented thing, so far as price is concerned, should be free of the monopoly."

Conceding that the patentee by statute has the exclusive right to use and to vend and to confer upon another such rights, " it goes beyond all reason," says the Court,

> to hold that, when the patentee has manufactured the article and fixed the value thereof, including his full royalty or consideration, a compensation for the right to use and sell the article, he may put the article on the market for sale by selling to jobbers and dealers who purchase for such purpose and pay the full price fixed, and still restrict them in the price they shall receive for their own property. It is an attempt to monopolize and control prices, and destroy competition, and when a

jobber or dealer takes a number of such articles for sale to others under such a restriction as to sales made by himself, there is at once a combination to fix prices and restrain trade in contravention of a sound public policy.

The hostility of the Court to such agreements is still more strongly put in this sentence: "Agreements, however designed and under whatever pretense made, having in view and for their object the monopoly or control of prices to the user and consumer and the destruction of competition, are void."

Thus, it seems quite certain that considerations of public policy were supreme in leading to the conclusion of the Court in this case.

The most famous of all price-maintenance cases is next to be considered — namely, the celebrated patent-medicine controversy known as the Sanatogen Case. It will be noted that the facts in this case are not essentially different from those in the case of Victor Co. *v.* The Fair, or in the case of National Phonograph Co. *v.* Schlegel. The trend of the argument is very similar to that in the case of Waltham *v.* Keene just discussed, and great stress is laid on the point that if the patentee has *in the act of sale received full compensation for his goods* he has thereby been deprived of all restrictive powers in subsequent sales, *notwithstanding contracts, notices, and agreements* to the contrary.[1]

The Bauer Chemical Co. was sole agent and licensee for the sale of Sanatogen in the United States by virtue of a contract with Bauer & Cie. of Berlin, Germany, the holders of the United States letters patent upon Sanatogen. On the original Sanatogen packages as sold by the Bauer Chemical Co. was the following inscription:

[1] Bauer *v.* O'Donnell (229 U. S. 1). Decided May 26, 1913.

NOTICE TO THE RETAILER

This size package of Sanatogen is licensed by us for sale and use at a price of not less than one dollar. Any sale in violation of this condition, or use when so sold, will constitute an infringement of our patent, under which Sanatogen is manufactured, and all persons so selling or using packages or contents will be liable to injunction and damages.

A purchase is an acceptance of this condition. All rights revert to the undersigned in the event of violation.

THE BAUER CHEMICAL CO.

O'Donnell, the proprietor of a retail drug store in the city of Washington ignored the stipulations of this notice and sold at a cut price. The ensuing suit was one of very great interest, for upon its result depended apparently the last hope of manufacturers to control resale prices through patent rights. The plaintiffs were aided in their struggle by special counsel on behalf of the Gillette Safety Razor Co. and the Victor Talking Machine Co., who filed briefs in their support.

The Court based its opinion in the form of an answer to this formal question: " May a patentee by notice limit the price at which future retail sales of the patented articles may be made, such article being in the hands of a retailer by purchase from a jobber who has paid to the agent of the patentee the full price asked for the article sold?"

No question exactly similar to this had before been presented to the Supreme Court.

The chief reliance of the plaintiff in this case was upon the decision in the Dick Case. The restriction that was sustained in that case, however, was one arising solely from the *right to use*, and it served to qualify in that case the title to the mimeographs, giving a right to use the machine only with certain specified supplies. Now in the Sanatogen case the plaintiffs attempted to qualify the title by granting a

right to use only under specified conditions, namely, the maintenance of the price at one dollar. But the Court held this a mere play upon words.

It is contended by argument that the notice in this case deals with the use of the invention, because the notice states that the package is licensed " for sale and use at a price of not less than one dollar," that a purchase is an acceptance of the conditions, and that all rights revert to the patentee in event of the violation of the restriction. But in view of the facts certified in this case, as to what took place concerning the article in question, it is a perversion of terms to call the transaction in any sense a license to use the invention. The jobber from whom the appellee purchased had previously bought, at a price which must be deemed to have been satisfactory, the packages of Sanatogen afterwards sold to the appellees. The patentee had no interest in the proceeds of the subsequent sales, no right to any royalty thereon, or to participating in the profits thereof. The packages were sold with as full and complete title as any article could have when sold in the open market, excepting only the attempt to limit the sale or use when sold for not less than one dollar. In other words, the title transferred was full and complete with *an attempt to reserve the right* to fix the price at which subsequent sales could be made. There is no showing of a qualified sale *for less than value for limited use with other articles only* as was shown in the Dick case. There was no transfer of a limited right to use this invention, and to call the sale a license to use is a mere play upon words.

The powers granted, then, under the *right to use* clause of the patent statute being manifestly insufficient to support the contention of the plaintiff, the question arises, does the right to vend as granted by the patent statute afford support to the contention? The Court held that it does not, in accordance with the Bobbs-Merrill ruling,[1] stating that,

[1] See *infra*, p. 184.

"Upon such facts as are now presented we think the right to vend secured in the patent statute is not distinguishable from the right of vending given in the copyright act," and that accordingly the right to vend having been exercised by the plaintiffs in their sales to the jobbers, it could not be further extended to cover subsequent sales. In conclusion, the Court sums up as follows: "The patentee or his assignee having in the act of sale received all the royalty or consideration which he claims for the use of his invention in that particular machine or instrument, it is open to the use of the purchaser *without further restriction* on account of the monopoly of the patentee."

This decisive dictum of the Court did not deter the Victor Talking Machine Co. in its program of attempted price maintenance. The method used was unique. To every machine sold by the Victor Co. was attached a notice reading in part as follows:

This machine is manufactured by us under our patents hereinafter noted and is licensed for use only, for the term of the patent having the longest time to run, and only with sound records, sound boxes, and needles manufactured by us; and our records and sound boxes are licensed only for use with our machines. Only the right to use the said machine is granted to Victor distributors and dealers for demonstrating purposes, with the right to the distributor to assign a like right to regularly licensed Victor dealers at the dealer's regular discount royalty, with the right to the dealers to convey the license to the public to use the said machine only when a royalty of not less than ——— shall have been paid, and upon consideration that all the conditions of license shall be strictly observed. A similar right is also granted to the distributor to convey to the public the right to use this machine under the same conditions. No license to use this machine is granted to the public until the full royalty shall have been paid. Title shall remain in the Victor Talking Machine Co.; also the right to repossess

the said patented goods upon the breach of any of the conditions, upon the repayment by the Victor Co. to the user of the royalty paid by him. . . .

Analysis of this license notice reveals three distinctive features. (1) All of the restrictions imposed by the Victor Co. are professedly based on patented rights alone, and are enforcible for a limited time only—that is, for the life of the patent having the longest term yet to run. (2) The consideration which the Victor Co. receives in parting with its machines is not a price but a royalty, and the full amount of the royalty is not secured until the machine is in the hands of the ultimate consumer. (3) There is no alienation of title by the manufacturer. Only the right to use is parted with upon the payment of royalty, this right, in the case of the distributors, being called a right to demonstrate.

In addition to this license notice, the Victor Co. utilized a form of special contract entered into with all its dealers, approximately 7000 in number. In this contract the terms of the " License Notice " are in substance repeated, and the dealer binds himself to the conditions of the license notice. The penalty stated in the contract was: "A breach of any of the conditions on the part of a distributor will render him liable, not only for an infringement of the patent, but to an action on the contract, or other proper remedy."

Macy & Co., a large mercantile establishment in New York, although not a party to any contract with the Victor Co., secured by indirect methods large quantities of Victor machines to which were affixed the above " license notice." These machines Macy & Co. sold at a cut price in violation of the license notice. Action was then taken in the courts by the Victor Co. to prevent the continuance of this practice, with the following result, as stated by the United States Supreme Court, April 9, 1917.[1]

[1] Straus *v.* Victor Talking Machine Co.; 243 U. S. 490.

First of all it is plainly apparent that this plan of marketing adopted by the plaintiff is, in substance, the one dealt with by this court in Dr. Miles Medical Co. *v.* Park & Sons Co., 220 U. S. 373, and in Bauer *v.* O'Donnell, 229 U. S. 1, adroitly modified on the one hand to take advantage, if possible, of distinctions suggested by these decisions, and on the other hand to evade certain supposed effects of them.

If we look through the words and forms, with which the plaintiff has most elaborately enveloped its purpose, to the substance and realities of the transaction contemplated, we shall discover several notable and significant features. . . . First, while as if looking to the future, the notice, in terms, imposes various restrictions as to title and as to the " use " of the machines by plaintiff's agents, wholesale and retail, and by the " unlicensed members of the public," for itself, the plaintiff makes sure that the future shall have no risks, for it requires that all it asks or expects at any time to receive for each machine must be paid in full before it parts with the possession of it.

Second, while in terms the " use " of each machine is restricted and forfeiture for failure to strictly comply with the many conditions and requirements of the notice is provided for, this system, elaborate to the extent of confusion, fails utterly to provide for entering any evidence of a qualified title in any public office or in any public record, and no requirement is found in it for reporting by users or licensees, who may remove from one place to another taking the machine with them, as would very certainly be required if the plaintiff intended to enforce the rights so elaborately asserted in this notice;—if the system were really a genuine provision designed to protect through many years to come the restricted right to " use " and the seemingly qualified title which it purports to grant to dealers and to the public, from being exceeded or departed from.

Third. The fact that under this system " at different times " " large numbers " of machines, as is alleged in the plaintiff's bill, have been covertly sold to the defendants by the plaintiff's

wholesale and retail agents at less than the price fixed for them, is persuasive evidence that the transaction is not what it purports on its face to be. If it were a reasonably guarded plan, really intended to keep the plaintiff in touch with each of its machines until the expiration of the patent of latest date, for the purpose of insisting upon its being used in the manner provided for in the "License Notice" the plaintiff's prompt and sufficient remedy for such an invasion of its right as is claimed in this case would be found in its sales department or rather in its license department, and not in the courts. That the plaintiff comes into court with a bill to enjoin the defendants from reselling machines secretly sold to them in large numbers by the plaintiff's agents indicates very clearly that at least until the exigency out of which this case grew, arose, the scheme was regarded by the plaintiff itself and by its agents simply as one for maintaining prices by holding a patent infringement suit *in terrorem* over the ignorant and the timid.

And finally, while the notice permits the use of the machines, which have been fully paid for, by "the unlicensed members of the general public," significantly called in the bill "the ultimate users," until "the expiration of the patent having the longest term to run," it provides that if the licensee shall not have failed to observe the conditions of the license, and the Victor Co. shall not have previously taken possession of the machine, as in the notice provided, then, perhaps sixteen years or more after he has paid for it and in all probability long after it has been worn out or become obsolete and worthless "it shall become the property of the licensee."

It thus becomes clear that this "license notice" is not intended as a security for any further payment upon the machine, for the full price, called a "royalty," was paid before the plaintiff parted with the possession of it; that it is not to be used as a basis for tracing and keeping the plaintiff informed as to the condition or use of the machine, for no report of any character is required from the "ultimate user" after he has paid the stipulated price; that, notwithstanding its

apparently studied avoidance of the use of the word "sale" and its frequent reference to the word "use," the most obvious requirements for securing a *bona fide* enforcement of the restrictions of the notice as to "use" are omitted; and that, even by its own terms, the title to the machines ultimately vests in the "ultimate users," without further payment or action on their part, except patiently waiting for patents to expire on inventions, which, so far as this notice shows, may or may not be incorporated in the machine. There remains for this "License Notice" so far as we can discover, the function only of fixing and maintaining the price of plaintiff's machines to its agents and to the public, and this we cannot doubt is the purpose for which it really was designed.

Courts would be perversely blind if they failed to look through such an attempt as this "License Notice" thus plainly is to sell property for a full price, and yet to place restraints upon its further alienation, such as have been hateful to the Law from Lord Coke's day to ours, because obnoxious to the public interest. The scheme of distribution is not a system designed to secure to the plaintiff and to the public a reasonable use of its machines, within the grant of the patent laws, but is in substance and in fact a mere price fixing enterprise, which, if given effect, would work great and wide-spread injustice to innocent purchasers, for it must be recognized that not one purchaser in many would read such a notice, and that not one in a much greater number, if he did read it, could understand its involved and intricate phraseology, which bears many evidences of being framed to conceal rather than to make clear its real meaning and purpose. It would be a perversion of terms to call the transaction intended to be embodied in this system of marketing plaintiff's machines a "license to use the invention."

Convinced as we are that the purpose and effect of this "License Notice" of plaintiff, considered as part of its scheme for marketing its product, is not to secure to the plaintiff any use of its machines, and as is contemplated by the patent statutes, but that its real and poorly concealed purpose is to

restrict the price of them, after the plaintiff had been paid for them and after they have passed into the possession of dealers and of the public, we conclude that it falls within the principles of Adams *v.* Burke, 17 Wall., 453; and of Bauer *v.* O'Donnell, 229 U. S., 1; that it is, therefore, invalid, and that the District Court properly held that the bill must fail for want of equity.

This vigorous blow at the validity of price maintenance based on patent rights was given strong reinforcement by the contemporaneous decision of the same court in the case of Motion Picture Patents Co. *v.* Universal Film Manufacturing Co. *et al.*[1] The facts of the case briefly stated were: The Motion Picture Patents Co. was the assignee of U. S. letters patent no. 707,934, granted in 1902 for improvements in projecting Kinetoscopes, and in accordance with its rights as assignee had by a "license agreement" granted to the Precision Machine Co. a right and license to manufacture and sell machines embodying the inventions described in the patent. In this agreement the Precision Machine Co., grantee, covenanted to sell its machines only under the condition that they be used "solely for exhibiting or projecting motion pictures containing the invention of letters patent no. 12,192, leased by a license of the licensor while it owns said patents and upon other terms to be fixed by the licensor and complied with by the user while the said machine is in use and while the licensor owns said patents."

In addition, the Precision Machine Co. agreed to affix to every machine sold by it the following notice:

[1] 243 U. S. 502.

SERIAL NO. ———

Patented.

The sale and purchase of this machine gives only the right to use it solely with moving pictures containing the invention of reissued patent no. 12,192, leased by a licensee of the Motion Picture Patents Co., the owner of the above patents and reissued patent, while it owns said patents, and upon other terms to be fixed by the Motion Picture Patent Company and complied with by the user while it is in use and while the Motion Picture Patents Company owns said patents. The removal or defacement of this plate terminates the right to use this machine.

The agreement further provided that the grantee should not sell any machine at less than the list price fixed by the Motion Pictures Patent Company, except to jobbers and others for purposes of resale, and that it would require such jobbers and others to sell at not less than the aforesaid list price.

Acting in accordance with the agreement, the Precision Machine Co. sold to the Seventy Second Street Amusement Co. a machine bearing the license notice quoted above. Soon afterwards the patent number 12,192, which was referred to in the notice and which affected only the films being used in the machine expired, and somewhat later the playhouse with the machine was leased to the Prague Amusement Co., which proceeded to use in the leased machine unpatented films acquired indirectly from the Universal Film Manufacturing Co. The plaintiff (The Motion Picture Patent Co.) thereupon notified the Prague Amusement Co. that its use of the leased machine without license constituted an infringement of the patent no. 707,934, and on the same day notice was also sent to the agent of the Universal Film Manufacturing Co. charging infringement of the same patent by supplying films for use upon the

machine in question. The subsequent suit was in support of these two contentions, wherefore the questions to be decided by the Supreme Court were:

First: May a patentee or his assignee license another to manufacture and sell a patented machine and by a mere notice attached to it limit its use by the purchaser or by the purchaser's lessee, to films which are no part of the patented machine, and which are not patented?

Second: May the assignee of a patent, which has licensed another to make and sell the machine covered by it, by a mere notice attached to such machine, limit the use of it by the purchaser or by the purchaser's lessee to terms not stated in the notice but which are to be fixed, after sale, by such assignee in its discretion?

The first of these does not vitally relate to price maintenance, so we need concern ourselves specifically only with that part of the decision dealing with the second. Says the Court:

The exclusive right to vend a patented article is derived from the same clause of the section of the statute which gives the exclusive right to "use" such an article, and following the decision of the *Button Fastener* Case, it was widely contended as obviously sound, that the right existed in the owner of a patent to fix a price at which the patented article might be sold and resold under penalty of patent infringement. But this Court in Bauer *v.* O'Donnell . . . refused to give such a construction to the Act of Congress, and decided that the owner of a patent is not authorized by either the letter or the purpose of the law to fix, by notice, the price at which a patented article must be sold after the first sale of it, declaring that the right to vend is exhausted by a single unconditional sale, the article sold being thereby carried outside the monopoly of the patent law and rendered free of every re-

striction which the vendor may attempt to put upon it. The statutory authority to grant the exclusive right to "use" a patented machine is not greater, indeed is precisely the same, as the authority to grant the exclusive right to "vend", and, looking to that authority, for the reasons stated in this opinion we are convinced that the exclusive right granted in every patent must be limited to the invention described in the claims of the patent and that it is not competent for the owner of a patent by notice attached to its machine to, in effect, extend the scope of its patent monopoly by restricting the use of it to materials necessary in its operation but which are not part of the patented invention, or to send its machines forth into the channels of trade of the country subject to conditions as to use or royalty to be paid to be imposed thereafter at the discretion of such patent owner. The patent law furnishes no warrant for such a practice and cost, inconvenience and annoyance to the public which the opposite conclusion would occasion forbid it.

It is argued as a merit of this system of sale under a license notice that the public is benefited by the sale of the machine at what is practically its cost and by the fact that the owner of the patent makes its entire profit from the sale of the supplies with which it is operated. This fact, if it be a fact, instead of commending, is the clearest possible condemnation of, the practice adopted, for it proves that under color of its patent the owner intends to and does derive its profit, not from the invention on which the law gives it a monopoly, but from the unpatented supplies with which it is used and which are wholly without the scope of the patent monopoly, thus in effect extending the power to the owner of the patent to fix the price to the public of the unpatented supplies as effectively as he may fix the price on the patented machine.

We are confirmed in the conclusion which we are announcing by the fact that since the decision of Henry *v.* Dick Co., 224 U. S. I. the Congress of the United States, the source of all rights under patents, as if in response to this decision, has enacted a law making it unlawful for any person engaged in

interstate commerce "to lease or make a sale or contract for sale of goods . . . machinery, supplies, or other commodities, whether *patented or unpatented*, for use, consumption or resale . . . or to fix a price charged therefor . . . on the condition, agreement or understanding that the lessee or purchaser thereof shall not use . . . the goods . . . machinery, supplies or other commodities of a competitor or competitors of the lessor or seller where the effect of that lease, sale or contract for resale, or such condition, agreement or understanding may be to substantially lessen competition or tend to create a monopoly in any line of commerce." (28 Stat. at Large, p. 730.)

Our conclusion renders it unnecessary to make the application of this statute to the case at bar which the Circuit Court of Appeals made of it but it must be accepted by us as a most persuasive expression of the public policy of our country with respect to the question before us.

It is obvious that the conclusions arrived at in this opinion are such that the decision in Henry *v.* Dick Co., 224 U. S. I. must be regarded as overruled.

Coming now to the terms of the notice attached to the machine sold to the Seventy-second Street Amusement Company under the license of the plaintiff and to the first question we have stated.

This notice first provides that the machine, which was sold to and paid for by the Amusement Company may be used only with moving picture films containing the invention of reissued patent No. 12,192, so long as the plaintiff continues to own this reissued patent.

Such a restriction is invalid because such a film is obviously not a part of the invention of the patent in suit; because it is an attempt, without statutory warrant, to continue the patent monopoly in this particular character of film after it has expired, and because to enforce it would be to create a monopoly in the manufacture and use of moving picture films, wholly outside of the patent in suit and of the patent law as we have interpreted it.

The notice further provides that the machine shall be used

only upon other terms (than those stated in the notice) to be fixed by the plaintiff, while it is in use and while the plaintiff "owns said patents." And it is stated at the bar that under this warrant a charge was imposed upon the purchaser graduated by the size of the theater in which the machine was to be used.

Assuming that the plaintiff has been paid an average royalty of $5 on each machine sold, prescribed in the license agreement, it has already received over $200,000 for use of its patented improvement, which relates only to the method of using the films which another had invented, and yet it seeks by this device to collect during the life of the patent in suit what would doubtless aggregate many times this amount for the use of this same invention, after the machines have been sold and paid for.

A restriction which would give to the plaintiff such a potential power for evil over an industry which must be recognized as an important element in the amusement life of the nation, under the conclusions we have stated in this opinion, is plainly void, because wholly without the scope and purpose of our patent laws and because, if sustained, it would be gravely injurious to that public interest, which we have seen is more a favorite of the law than is the promotion of private fortunes.

If there remains any doubt whatsoever as to the utter futility of attempting to maintain prices through patent rights, it must be dispelled by the following case in which the Court views the whole question very comprehensively and states in terms not to be debated further its uncompromising aversion from the theory and practice of price maintenance as they are at present known to the Court. So notable is this case for its atmosphere of finality, that it may well be doubted if further litigation involving price maintenance will be attempted in the absence of new statutory enactments. The decision in this case was handed down March 4, 1918. The facts are briefly stated:

The American Graphophone Co., a West Virginia corporation, as assignee of certain letters patent of the U. S., was the sole manufacturer of Columbia Graphophones and records, and the Columbia Graphophone Co. was their general sales agent. The American Co., through its agent, employed in the marketing of its products a system of price maintenance effected by the use of special contracts entered into with all dealers in which the dealers, in consideration of special prices so-called, pledged themselves to maintain the official list of reselling prices fixed from time to time at the instance of the American Co. The Boston Store of Chicago had entered into such a contract, containing the following provisions:

"NO JOBBING PRIVILEGES EXTENDED UNDER THIS CONTRACT."

Notice to purchasers of Columbia Graphophones, Grafonolas, Records and Blanks.

All "Columbia" Graphophones, Grafonolas, Records, and blanks are manufactured by the American Graphophone Co. under certain patents and licensed and sold through its sole sales agent, the Columbia Phonograph Co., subject to conditions and restrictions as to the persons to whom and the prices at which they may be resold by any person into whose hands they come. Any violation of such conditions or restrictions make the seller or user liable as an infringer of said patents.

After reading the foregoing notice and in consideration of current dealers' discounts given to us by the Columbia Phonograph Co., we hereby agree to take any Columbia product received by us from said company, either directly or through any mediary, under the conditions and restrictions referred to in said notice and to adhere strictly and be bound by the official list prices established from time to time by said Company and that we will neither give away, sell, offer for sale, nor in any way dispose of such goods, either directly or through any inter-

mediary, at less than such list prices, nor induce the sale of such goods by giving away or reducing the price of other goods, nor sell or otherwise dispose of any of said goods, directly or indirectly, outside of the United States, and we understand that a breach of this agreement will amount to an infringement of said patents and subject us to a suit and damages therefor. We admit the validity of all patents under which said product is manufactured and hereby covenant and agree not to question or contest the same in any manner whatsoever. We further understand and agree that this license extends the right to market said Columbia product from the below mentioned address only, and that a separate contract is required to market said product from a branch store or stores, or through an agency or agencies at any other point.

These provisions were violated by the Boston Store, and the American and Columbia Companies consequently brought suit to enforce the agreement as part of the remedy given by the patent laws to protect the patent rights of the American Company. Regarding the points submitted by the lower court for adjudication, the Supreme Court said: [1]

In a general sense the questions involve determining whether the right to make the price maintenance stipulation in the contract stated and the right to enforce it were secured by the patent law, and if not, whether it was valid under the general law, and was within the jurisdiction of the court on the one hand because of its authority to entertain suits under the patent law or its power on the other to exercise jurisdiction because of diversity of citizenship. We at once say, despite insistence in the argument to the contrary, that we are of opinion that there is no room for controversy concerning the subjects to which the questions relate, as every doctrine which is required to be decided in answering the questions is now

[1] Boston Store of Chicago *v.* American Graphophone Co.: U. S. S. C., March 4, 1918, 246 U. S. 8.

no longer open to dispute as the result of prior decisions of this court, some of which were announced subsequent to the making of the certificate in this case.

A review of the following cases is then made by the court: Bobbs-Merrill Co. *v.* Straus; Dr. Miles Medical Co. *v.* Park and Sons Co.; Henry *v.* A. B. Dick Co.; Bauer *v.* O'Donnell; Straus *v.* Victor Talking Machine Co.; and Motion Picture Patent Co. *v.* Universal Film Manufacturing Co. And continuing, the court says:

Applying the cases thus reviewed there can be no doubt that the alleged price-fixing contract disclosed in the certificate was contrary to the general law and void. There can be equally no doubt that the power to make it in derogation of the general law was not within the monopoly conferred by the patent law and that the attempt to enforce its apparent obligations under the guise of a patent infringement was not embraced within the remedies given for the protection of the rights which the patent law conferred.

Thus concluding, it becomes we think unnecessary to do more than say that we are of opinion that the attempt in argument to distinguish the cases by the assumption that they rested upon a mere question of the form of notice on the patented article or the right to contract solely by reference to such notice is devoid of merit since the argument disregards the fundamental ground upon which, as we have seen, the decided cases must rest. Moreover, so far as the argument proceeds upon the assumption of the grave disaster which must come to the holders of patent rights and articles made under them from the future application of the doctrine which the cases establish, it must be apparent that if the forebodings are real the remedy for them is to be found not in an attempt judicially to correct doctrines which by reiterated decisions have become conclusively fixed, but invoking the curative power of legislation.

To the supporters of the doctrine of price maintenance based on patent rights, the only balm that remains after this long series of cases is the recommendation of the court that they go and "invoke the curative power of legislation."

With respect to copyrights, the decisions affecting price maintenance have been few. It now seems definitely established that the holder of a copyright has practically the same standing as does the patentee with respect to price restrictions. The standard case is that of Bobbs-Merrill Company *v.* Straus, decided in 1908 (210 U. S. 239).

The Bobbs-Merrill Company was the owner of a copyright upon "The Castaway." Printed immediately beneath the copyright notice on the page in the book following the title-page was inserted the following notice:

> The price of this book at retail is one dollar, net. No dealer is licensed to sell it at a less price, and a sale at a less price will be treated as an infringement of the copyright.
>
> THE BOBBS-MERRILL CO.

Ninety per cent of the copies of the books handled by Macy & Co. were purchased by them at wholesale at a price below the retail price by about forty per cent. At the time of purchase the latter company knew that the book was copyrighted, and was aware of the terms of the notice given above, yet advertised and sold the book at 89 cents per copy.

The publishing company based its claim for reselling rights chiefly upon the analogy drawn from assumed patent rights, alleging that previous court decisions had recognized rights of price maintenance in patentees, and that by analogy similar rights should inhere in holders of copyrights.

Mr. Justice Day, writing the opinion of the court, concludes, however, that the analogy is false in the premises, for the court has given no such rights to patentees. He

disposed of the Bement *v.* National Harrow Co. case by saying:

that suit was between the owners of the letters patent as licensor and licensee, seeking to enforce a contract as to the price and terms on which the patented article might be dealt with by the licensee. The case did not involve facts such as in the case now before us, and concerned a contract of license sued upon in the state court, and, of course, does not dispose of the questions to be decided in this case.

Furthermore, the court falls back upon the decision of Judge Lurton in the case of Park & Sons *v.* Hartman: "There are such wide differences between the right of multiplying and vending copies of a production protected by the copyright statute, and the rights secured to an inventor under the patent statutes, that the cases which relate to the one subject are not altogether controlling as to the other."

The court bases its decision on statutory construction solely, refusing to consider what powers might arise from copyright should the holder thereof resort to contract limitation, or license agreement controlling the subsequent sales of the book. The main purpose of the copyright law is construed to be the protection of the authors in the right of multiplying copies of their works; but while protecting him in the right to multiply and vend his works, does not create the right to impose by notice, such as is disclosed in this case, a limitation at which the book shall be sold at retail by future purchasers with whom there is no privity of contract.

Subsequent decisions of the court, though not directly involving copyright powers relative to price maintenance, do by very convincing implication virtually establish the principle that in no way can maintenance of prices be estab-

lished by recourse to real or fancied rights arising from the United States copyright laws.

With respect to proprietary articles and trade-marked goods, the tenor of the court decisions has been quite uniform. No device for maintaining prices in such lines has yet met with positive approval from the federal courts. Even the indirect methods, almost without exception, have been condemned.

The first case arose from the famous "tri-partite" plan entered into by the Proprietors' Association of America, the National Wholesale Druggists' Association, and the National Association of Retail Druggests.[1] The plan was formulated at a convention of the wholesalers in Chicago in 1900, the proprietors participating, and was adopted by all three associations. The adherence and concerted action of the members of each association were secured by direct appeal and individual assent. As a result of it the proprietors sold only at uniform and fixed prices to those wholesalers and jobbers who agreed to maintain prices, and not sell to aggressive cutters, the recognized list of such jobbers being furnished to the proprietors by the chairman of the proprietary committee of the wholesalers, and the list of the aggressive cutters, as reported by local associations of retailers, being made up and sent out to jobbers and proprietors by the secretary of the National Retailers. If a wholesaler failed to regard the list, he was promptly reported, and his name added to it.

In 1902, Resolution *C* was adopted:

That the Secretary be instructed to request all manufacturers of chemicals, pharmaceuticals, plasters, dressing, and like products, handled by the drug trade, to desist from selling to ag-

[1] Jayne *v.* Loder (149 Fed. Rep. 21). Dec., 1906.

gressive cutters, or suppliers of cutters, when solicited to do so by the respective local associations; and that the retail druggist shall be made acquainted with the responses to such requests, in such manner as the executive committee may deem best.

The court first attacks the combination element in this arrangement, saying that

undoubtedly the originator and compounder of a proprietary medicine may shape his own policy, and sell, and withhold from selling as he pleases, according to supposed self-interest or whim; fixing the prices and naming the terms and conditions at and upon which alone he will do so, refusing to those who do not comply. And so far as this is confined to his own goods, and pursued by independent and individual action, it cannot be challenged. It is *quite a different matter*, however, *when two or more combine . . . , it is the joining together of numbers that counts.*

This joining together on the part of the druggists is confidently asserted by those who should know to have cost the country about 90 million dollars within a space of six years.

It is accordingly on broad grounds of public policy, rather than on considerations of price maintenance as such, that the court decides adversely in this case. One is led to think by the argument in the decision that the court would have adjudged as legal the fixing of resale prices by the proprietor acting independently. *Only when a number* of proprietors themselves combined, as well as the other factors, did the arrangement become illegal. The vitiating element was that of combination.

The next case is much more definite and decisive in its condemnation of resale price-fixing.[1]

[1] John D. Park & Sons Co. *v.* Hartman (153 F. R. 24). Decided March 14, 1907.

The Hartman Co. were manufacturers of certain medicines of secret formulas which they put up and sold under distinctive dress and trade-mark. All jobbers and dealers handling the medicines were required to bind themselves by contract to sell at prices fixed by the manufacturer, and the enforcement of the contracts was facilitated by the use of serial numbers upon the packages as well as by a requirement that retailers should affix their signatures to such medicines as were sold by them. Park & Sons, failing to enter such agreement, but continuing to sell the medicines at any price they chose, were sued by the Hartman Co. on the ground that such action by Park & Co. was an infringement of certain rights growing out of the possession of trade secrets; that the possession of secret formulas in the manufacture of medicines carried with it the right to make restrictive contracts in the assignment of using and selling rights to the medicines. The court refused to abide by this view, and held that the action of Hartman was in restraint of trade, and violative of the anti-trust laws. Thus vanished the possibility of price maintenance in regard to proprietary or secret-process remedies by the method of contract or notice.

If any doubt remained as to the legal status of resale price-fixing in proprietary goods, it was completely dissipated in the case of Dr. Miles Medical Co. *v.* John D. Park & Sons Co.[1]

Dr. Miles Medical Co., a corporation of Elkhart, Indiana, was the proprietor or manufacturer of certain medicines prepared by means of secret methods and formulas and identified by distinctive packages, labels and trade-marks. It had established an extensive trade, both in the United States and in certain foreign countries. In the case of each

[1] 220 U. S. 373. Decided April 3, 1911.

remedy it fixed not only the price at which its own sales were made but also the wholesale and retail prices. It depended for the maintenance of these prices upon specific contracts drawn up with each and every one of its wholesalers. The provisions of the contract were in the main as follows: The Dr. Miles Medical Co. designated its wholesalers as consignees to whom the goods were consigned for sale, and stipulated that such consignees should not be given title to the goods until the goods were sold in accordance with the provisions of the contract. Following in the contract is a list of prices to which the dealers were required to adhere. The contract attempted to make of the dealers agents only and their profits were to be paid in the form of commissions on their sales. It is further stipulated that the wholesalers or consignees should not sell goods to retailers other than those specified by The Dr. Miles Medical Co. Semi-monthly reports were also required of the consignees in which were itemized the facts of every sale as to price, parties, and even the serial numbers on the package sold.

Similarly, contracts were required of all retailers handling the medicines in question, said contracts fixing the prices and methods, and stipulating as to permitted discounts, premiums, trading stamps, etc.; use of the last two devices being specifically forbidden. The contract went so far as not only to threaten severance of business relations but also to impose a fine of $25.00 for each violation of the provisions. Such contracts were entered into with over 400 jobbers and wholesalers and 25,000 retail dealers in proprietary medicines in the United States.

Now the John D. Parks & Sons Co. had entered into no such contract. They had, however, by indirect methods been able to secure the medicines of the Miles Medical Co. and were advertising and selling them in Cincinnati at cut prices. The Miles Co. alleged that the medicines were

secured from its agents by means of false and fraudulent representations and statements and by surreptitious and dishonest methods and by persuading and inducing a violation of their contracts. It furthermore alleged that the practices complained of had resulted in seriously disorganizing its business in certain territories and had occasioned to the company serious financial losses.

In support of its system of price control, it maintained that its contracts were *contracts of agency* and not contracts of sale, that the dealers were merely *distributing agents* and, as such, properly subject to any price restrictions that the Proprietor might see fit to impose upon them. Furthermore, that trade secrets and articles embodying them were property monopolies and that such contracts with respect to them were therefore valid. It went further and argued that the right of monopoly in inventions, discoveries and writings is the foundation of the patent and copyright laws, and that by analogy a similar right of monopoly should obtain in articles made under trade secrets, their ingredients and proportions of ingredients and manufacturing processes being unknown and undisclosed.

The court in its decision disposed of the agency aspect of the agreement by holding that it was clearly an agreement looking to sale and not to agency. "The so-called retail agents are not agents at all, but are contemplated purchasers who buy to sell again, that is, retail dealers." The implication is that the court will not be restrained from looking into and condemning illegal practices when such practices are committed under the cloak of forms which are in themselves legal.

Without, then, laying much stress on the forms of the agreements, the court goes into a discussion of what must be the effects of the agreements, the greater emphasis being laid upon this point. The effects are found to be such as

are restraining in their influence upon trade. They eliminate absolutely every vestige of competition in the articles manufactured by the Dr. Miles Medical Co. and not as between a few parties only or in a limited territory, but throughout the country as a whole, affecting every jobber and retailer within its borders. The arrangement, then, is manifestly one in restraint of trade, and as such falls within the condemnation of the federal anti-trust acts. On such broad grounds of public policy the court adjudged the arrangement illegal. The allegation by the Proprietor that it was justifiable by an analogy drawn from the rights arising under the patent and copyright laws, the court denied, holding that no considerations involving the patent and copyright laws could apply in this case.

The principal point of the decision is probably summed up in these words:

Where commodities have passed into the channels of trade and are owned by dealers, the validity of agreements to prevent competition and to maintain prices is not to be determined by the circumstances whether they were produced by several manufacturers or by one, or whether they were previously owned by one or by many. *The complainant, having sold his product at prices satisfactory to himself, the public is entitled to whatever advantage may be derived from competition in the subsequent traffic.*

The most recent decision under this reading, although affecting our problem only indirectly, has, nevertheless, been hailed as a distinct victory by the advocates of price maintenance. If it be upheld by the Supreme Court, as seems likely, it will assume a deep significance unquestionably, and go to show that it is after all not so much the principle of price maintenance which the courts are attacking as the forms which so far have been used to attain it.

The case of the Great Atlantic & Pacific Tea Co. *v.* Cream of Wheat Co. was disposed of in the United States Circuit Court of Appeals of New York, Nov. 10, 1915.[1]

The Cream of Wheat Co. deals in the manufacture and sale of the well-known cereal, *Cream of Wheat.* This cereal is not in the strictest sense a specially manufactured article. It is a by-product in flour-making, and consists only of the middlings left over after the bran and flour have been subtracted from the wheat. These middlings are cleaned and purified by the Cream of Wheat Co. and put upon the market under their trade name. In 1913 the company published a scheme of sales in which it announced that it reserved the right to refuse to sell to anybody who failed to comply with any request made for the good of the trade or the consumer, and would confine its sales "exclusively" to wholesalers. Sales were no longer to be made directly to consumers, retailers, chain stores or department stores. No contracts or agreements with respect to the resale prices would be asked for, but nevertheless dealers were requested to keep retail prices at the level recommended by it. This request, taken in conjunction with the reserved right to cease selling to anyone who did not comply with requests, was in effect saying plainly enough, "keep up the retail price or we will stop supplying you."

Notwithstanding, however, this published sales plan, the Cream of Wheat Co. did sell to the Great Atlantic and Pacific Tea Co. at wholesale rates and in large quantities, though the A. & P. Tea Co. is a chain of retail stores. The sales were made, however, on condition that the chain would not sell the product at less than 14 cents per package. In January, 1915, the chain began ignoring this condition and sold Cream of Wheat at its "Economy Stores" at 12 cents per

[1] 227 F. R. 46.

package. Whereupon the Cream of Wheat Co. refused to sell any more cereal to the chain, and in addition sent out circulars to the jobbing trade asking them not to sell to the offender. Though the latter act was not very effective, the former was to the extent that it deprived the A. & P. Tea Co. of the carload rates which it formerly enjoyed, which meant that the 12 cents per package price could no longer be indulged in except at a loss. This caused the A. & P. Tea Co. to apply for an injunction under the Clayton and Sherman Acts, forcing the Cream of Wheat Co. to sell to it at the disadvantageous carload rate of $3.95 per case.

The plaintiff's syllogisms in support of the demand for relief are formulated by the court as follows:

(1) Defendant has a monopoly in Cream of Wheat;
(2) Through such monopoly it fixes the resale price of that article; therefore,
(3) It prevents competition in Cream of Wheat, and violates the body of Sec. 2. (Clayton Act.)

Again:

(1) Preventing competition is restraint of trade,
(2) Defendant does prevent competition; therefore,
(3) It restrains trade, and is not within the exception of Sec. 2. (See appendix.)

Taking up *seriatim* the parts of the above propositions, the court held with respect to the first that although the defendant did possess a monopoly in Cream of Wheat, it was a perfectly legal monopoly resting upon trade-mark rights. It was, moreover, a "monopoly of a creator"; "something which is not and never has been within the prohibition of any law."

The court also denies the truth of the minor premise—that the defendant fixes the resale price: "Mere abstention from dealing cannot *per se* be price-fixing, because the

price is not made to depend upon any contract or agreement." The premises being thus invalidated, the court does not consider the conclusion of the first proposition.

Concerning the second syllogism, the court held that any and every species of competition need not be in restraint of trade. The same rule of reason that has come to be invoked in applications of the Sherman Act is also to be invoked in the application of the Clayton Act. At this point the court makes a statement which, coming from a federal judge, is, to say the least, very unique:

The only competition prevented or sought to be prevented by defendant's acts, is that of Cream of Wheat *against itself;* the only trade restrained is the commercial warfare of a large buyer against small ones, or that of a merchant who, for advertising purposes, may sell an article at a loss, in order to get customers at his shop, and then persuade them to buy other things at a compensating profit. That competition as encouraged by statutes and decisions, does not include such practices, has been sufficiently shown in Fisher Flouring Mills *v.* Swanson, 76 Wash., 649.

Judicial notice of the motives and methods of the price-cutter had not before been taken in so emphatic a manner except in the Washington case mentioned, Fisher *vs.* Swanson.

The economic results of predatory price-cutting are also considered at some length, as follows:

Cream of Wheat is not a necessity, it is not even a staple article of commerce. Its continued existence depends upon defendant's ability to control the marketing of its own product. The doing of what plaintiff wishes would take from every groceryman near an "Economy Store" the last incentive to buy any Cream of Wheat, and collectively such grocery keepers are more important to the public and the defendant, than is the

plaintiff. If injunction were granted, defendant and many retailers would be injured, and the microscopic benefit to a small portion of the public would last only until plaintiff was relieved from the competition of the 14c grocers,—when it, too, would charge what the business would normally and naturally bear. In short, *it is plaintiff and not defendant* that pursues methods, whose hardship and injustice have often been judicially commented upon.

The question now arises, did the Cream of Wheat Co. have the right arbitrarily to select its customers without being guilty of restraint of trade? The ruling of the court is interesting:

How it can be called substantial and unreasonable restraint of trade to refuse to deal with a man who avowedly is to use his dealing to injure the vendor; when the vendor makes and sells only such an advertisement begotten article as Cream of Wheat, whose fancy name needs the nursing of carefully handled sales to maintain an output of trifling moment in the food market,—is beyond my comprehension.

The only alternative to free choice of customers is compulsory sales, and compulsory sales would be tantamount to confiscation, not confiscation for the good of the public as a whole, but for the benefit of a certain few individuals. Said the court:

If defendant's actual scheme of interstate business is unlawful, the United States certainly, and now perhaps an indivdual, can put it out of business; but neither the nation, nor any individual, can take away its property, with or without compensation, for the private use of any one.

By way of summary, it may be said in general that, with respect to patented articles, their sale having once been accomplished, no right or royalty in the article sold being

retained by the patentee and no profits from the sale shared by him, the resale price thereof cannot be limited or fixed, either by notice attached to the article or by contract. It must not be inferred from this that conditional sales whereby title is retained in the seller pending the performance of a condition, or transfer by license agreement when such conditional sale or license transfer is for the purpose of maintaining prices, would be tolerated by the federal courts. If there is any device by which a patentee or his assignees can legally maintain resale prices, it yet remains to be brought to the attention of the court.

To copyrighted articles the same general proposition applies as applies to patented goods.

With respect to proprietary medicines or trade-marked goods, when an outright sale of the goods is made, the manufacturer has parted with all property right in the article, and cannot thereafter control the resale price of his product in the hands of the vendee.

Seemingly the nearest approach to a successful indirect maintenance of prices is by the method of withholding supplies of goods from those dealers who cut prices. The decision of the court in the Cream of Wheat case indicates that this plan may possibly be legal, provided it be unaccompanied by any conspiracy with jobbers or dealers.[1] Even this plan, however, seems likely to be opposed by the Federal Trade Commission. At this writing (May, 1918) action has been taken by the Commission to restrain virtually a score of specialty manufacturers, including such prominent companies as Colgate & Co., and Cluett, Peabody & Co.,

[1] Since the above was written, the U. S. District Court for the eastern district of Virginia has handed down a decision (Oct. 29, 1918) upholding the Colgate plan of price maintenance which was to refuse goods to all price-cutters. These refusals were unattended by agreements or conspiracies with dealers (253 F. R. 522).

from the exercise of this method of price maintenance. If the Commission is successful, the last pathway toward a possible maintenance of prices will be closed, unless Congress can be persuaded to reopen it by the enactment of new legislation.

ADDITIONAL REFERENCES

(Bearing upon Legal Status)

Harvard Law Review, vol. xxvii, p. 139. Article by E. S. Rogers.

Report, Bureau of Corporations, 1915. *Trust Laws and Unfair Competition.*

University of Penna. Law Rev., Nov., 1914. Article by C. L. Miller.

Gilbert H. Montague, *Unfair Methods of Competition*, New York, 1917.

American Fair Trade League. Report on *Legal Status of Price Maintenance.* Prepared by C. L. Miller, Pub., Jan. 15, 1916.

H. R. Tosdal, "Price Maintenance," *American Ec. Rev.*, vol. viii, p. 35.

Joseph A. Minturn, *Price Regulation under Patents*, Indianapolis, 1916.

W. L. Slichter, "The Cream of Wheat Case," *Pol. Sci. Quarterly*, vol. xxxi, pp. 391-412.

William F. Gephart, *Some Economic and Legal Aspects of Fixed Prices.* Washington Univ. Studies, 1916, pp. 161-181.

A most excellent discussion of the pros and cons relative to the legal status of price maintenance in this country and abroad may be found in the *Hearings before the Interstate and Foreign Commerce Committee* (House), on H. R. 135-68, Jan. 5 to 11, 1917; pp. 4-79; and pp. 434-487.

APPENDIX

Part I

Those portions of the Sherman Anti-Trust Act of 1890 which may be said to relate to the problem of price maintenance are as follows:

Sec. 1. "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several states, or with foreign nations," is hereby declared to be illegal. . . . .

Sec. 2. "Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several states, or with foreign nations," shall be deemed guilty of a misdemeanor. . . . .

Sec. 3. "Every contract, combination in form of trust or otherwise, or conspiracy, in restraint of trade or commerce in any territory of the United States or of the District of Columbia, or in restraint of trade or commerce between any such territory and another, or between any such territory or territories and any state or states or the District of Columbia, or with foreign nations, or between the District of Columbia and any state or states or foreign nations, is hereby declared illegal."

Part II

The Federal Trade Commission Act of Sept. 26, 1914, is not more specific in its general prohibitions than the Sherman Act. Should the Commission take official action regarding price cutting or price control, it would be through the following general provision:

Sec. 5. "That unfair methods of competition in Commerce are hereby declared unlawful."

"The Commission is hereby empowered and directed to prevent persons, partnerships, or corporations, except banks, and common carriers subject to the Acts to regulate commerce, from using unfair methods of competition in commerce."

Part III

Certain indirect methods of maintaining prices are expressly forbidden by the following sections of the Clayton Act. (Oct. 15, 1914):

Sec. 2. "That it shall be unlawful for any person engaged in commerce, in the course of such commerce, either directly or indirectly to discriminate in price between different purchasers of commodities which commodities are sold for use, consumption, or resale within the United States or any Territory thereof or the District of Columbia or any insular possession or other place under the jurisdiction of the United States, *where the effect of such discrimination may be to substantially lessen competition or tend to create a monopoly* in any line of commerce: *Provided,* That nothing herein contained shall prevent discrimination in price between purchasers of commodities on account of differences in the grade, quality, or quantity of the commodity sold, or that makes only due allowance for difference in the cost of selling or transportation, or discrimination in price in the same or different communities made in good faith to meet competition: *And provided further,* That nothing herein contained shall prevent persons engaged in selling goods, wares, or merchandise in commerce from selecting their own customers in *bona fide* transactions and not in restraint of trade.

Sec. 3. "That it shall be unlawful for any person engaged in commerce, in the course of such commerce, to lease or make a sale or contract for sale of goods, wares, merchandise, machinery, supplies or other commodities, whether patented or unpatented, for use, consumption or resale within the United

States or any Territory thereof or the District of Columbia or any insular possession or other place under the jurisdiction of the United States, or fix a price charged therefor, or discount from, or rebate upon, such price, on the condition, agreement or understanding that the lessee or purchaser thereof shall not use or deal in the goods, wares, merchandise, machinery, supplies or other commodities of a competitor or competitors of the lessor or seller, where the effect of such lease, sale, or contract for sale or such condition, agreement or understanding may be to substantially lessen competition or tend to create a monopoly in any line of commerce."

Part IV

The forms of price-maintenance bills submitted to Congress have been numerous and varied. The one now pending, which is but a slight modification of the Stevens Bill, is given in full below: (The Stevens-Ashurst Bill, H. R. 13568, 64th Cong., 2d Ses.).

" That in any contract for the sale of articles of commerce to any dealer, wholesale or retail, by any grower, producer, manufacturer, or owner thereof, under the trade mark or special brand, hereinafter referred to as the 'vendor,' it shall be lawful for such vendor, whenever the contract constitutes a transaction of commerce among the several States or with foreign nations, or in any territory of the United States, or in the District of Columbia, or between any such territory and another territory, or between any such territory or territories and any States or the District of Columbia or with a foreign nation or nations, or between the District of Columbia and any State or States or a foreign nation or nations, to prescribe the uniform prices and manners of settlement at which the different qualities and quantities of each article covered by such contract may be resold:

" Provided, that the following conditions are complied with:

"(a) Such vendor shall not have any monopoly or control of the market for articles belonging to the same general class of

merchandise as such article or articles of commerce as shall be covered by such contract of sale; nor shall such vendor be a party to any agreement, combination or understanding with any competitor in the production, manufacture or sale of any merchandise in the same general class in regard to the price at which the same shall be sold, either to dealers at wholesale or retail or to the public.

"(b) Such vendor shall file at the office of the Federal Trade Commission a statement setting forth the trademark or special brand owned or claimed by such vendor in respect of such article or articles of commerce to be covered by such contract of sale, and also, from time to time, as the same may be adopted or modified, a schedule setting forth the uniform price of sale thereof to dealers at wholesale, and the uniform price of sale thereof to dealers at retail from whatever source acquired, and the uniform price of sale thereof to the public, and upon filing such statement such vendor shall pay to the Federal Trade Commission a registration fee of $10. Prices set forth in such schedule and made in any contract pursuant to the provisions of this act shall be uniform to all dealers in like circumstances, differing only as to grade, quality or quantity of such articles sold, the point of delivery and the manner of settlement, all of which differences shall be set forth in such schedule; and there shall be no discrimination in favor of any vendee by the allowance of a discount, rebate or commission for any cause, or by grant of any special concession, or by any other device whatsoever.

"(c) Such contracts for the sale of such article or articles of commerce may provide for seasonal disposal sales, twice yearly at appropriate times, by dealers at retail, during which periods, duly set forth in such statements or in such schedule of prices as shall be filed by such vendor, such dealers at retail may sell such article or articles of commerce for a price other than the uniform price as set forth in the schedule provided in the preceding paragraph (b): Provided, That such article or articles of commerce shall have first been offered to the vendor, by such dealer at retail, by written offer, at the price

paid for the same by such dealer, and that such vendor, not less than thirty days prior to the date set forth for the next seasonal disposal sales, after reasonable opportunity to inspect such article or articles, shall have refused or neglected to accept such offer.

"(d) Any article of commerce or any carton, package, or other receptacle inclosing an article or articles of commerce covered by such contract and in the possession of a dealer may be sold for a price other than the uniform price for resale by such dealer for such quality and quantity as set forth in the schedule provided in the preceding paragraph (b): First, if such dealer shall cease to do business and the sale is made in the course of winding up the business of such dealer, or if such dealer shall have become bankrupt or a receiver of the business of such dealer shall have been appointed: Provided, That such articles or articles of commerce shall have first been offered to the vendor thereof by such dealer or the legal representative of such dealer by written offer at the price paid for the same by such dealer, and that such vendor, after reasonable opportunity to inspect such article or articles, shall have refused or neglected to accept such offer; or, Second, if such article of commerce or contents of such carton, package or other receptacle shall have become damaged, deteriorated or soiled: Provided, That such damaged, deteriorated or soiled article shall have first been offered to the vendor by such dealer by written offer at the price paid for the same by such dealer, or at the option of such vendor, in exchange for similar articles not damaged, deteriorated or soiled, and that such vendor, after reasonable opportunity to inspect such article or articles, shall have refused or neglected to accept such offer, and that such damaged, deteriorated or soiled articles shall thereafter only be offered for sale by such dealer with prominent notice to the purchaser that such article is damaged, deteriorated or soiled, and that the price thereof is reduced because of such damage."

ERRATA

1. On page 166 the entire paragraph is made to appear as a quotation from Adams *v.* Burke. In fact only the first sentence is from that case. The quotation in the second sentence is from the Waltham *v.* Keene decision, p. 232, being requoted from the Dick case. The third quotation in the paragraph is from the Waltham *v.* Keene decision, p. 233. Moreover, the italics throughout the paragraph are the author's.
2. The italics in the quotation on p. 187 are the author's.
3. The italics in the quotation on p. 191 are the author's.
4. On page 165, second line, the word "majority" as used indicates only a majority of the Justices participating in the case.

VITA

The author was born April 17, 1889, in Burke County, North Carolina. His early education was acquired at Penelope Academy, North Carolina, and at the Male High School of Louisville, Kentucky. His undergraduate work was done at Wake Forest College, from which institution he received the A.B. degree in 1911.

His graduate studies were pursued in the School of Political Science of Columbia University, where he was in residence from September, 1913, to June, 1916. His major subject was Economics, especial attention being devoted to those portions of it outlined by the following courses: History of Economic Theory, Finance, The Railway Problem, as presented by Professor Seligman; The Labor Problem, The Trust Problem, Classical Economic Theory, as presented by Professor Seager; Modern Economic Theory, Business Cycles, as given by Professor Mitchell. Particularly valuable were the seminar courses directed by Professors Seligman and Seager, which he attended for two years, in which time he led discussions twice — one on the Federal Reserve System, and one on Resale Price Maintenance. He acted as assistant to Professor Seager in 1915 and to Professor Ripley during the spring term of 1916.

For two years, 1916-18, he was Assistant Professor of Economics in Miami University, Ohio. At present he is Assistant Professor of Economics in Hunter College, New York City.